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International Economic & Energy Weekly

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16 August 1985

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Perspective

Commercial Bank Lending: A Growing Dichotomy [redacted] 25X1

Since early 1984 it appears commercial banks are treating individual developing and East European countries differently in their lending. While the overall pace of bank lending continues to decelerate, creditworthy countries such as Thailand, Algeria, South Korea, and East Germany still enjoy access to international capital markets and have raised considerable amounts this year—often at favorable rates. For those countries experiencing foreign payments difficulties, however, there is little hope for any significant upturn in voluntary lending over the near term. [redacted] 25X1

To generate savings on debt service costs, we believe many borrowers will move away from syndicated loans and toward security-related transactions—floating rate notes, bonds, and commercial paper—which are less costly because the borrower raises funds directly from the capital markets. Such financing has provided a sizable portion of the $7 billion borrowed by Asian LDCs so far this year. Traditional syndication borrowers such as Thailand, Malaysia, and Indonesia have turned increasingly to security-backed transactions to fill their borrowing requirements at below LIBOR rates. In contrast, the market for syndicated loans is shrinking. It remains strong in Eastern Europe, however, where there has been a dramatic resurgence in borrowing. Syndicated credits to Bulgaria, Czechoslovakia, East Germany, and Hungary thus far in 1985 are approaching the total for the region over the past three years. Nonetheless, commercial banks are shunning troubled debtors such as Poland, Yugoslavia, and Romania. [redacted] 25X1

The prospects of most borrowers remain severely constrained with most new lending associated with rescheduling agreements and IMF programs. For debt-troubled LDCs, short-term trade finance remains the only source of voluntary commercial bank lending. As a result, LDCs continue to experience a net outflow of funds as these new short-term trade credits are being more than offset by repayments of existing loans. New money packages arranged as part of IMF-supported adjustment programs brought considerably more money into the LDCs—$9 billion to Brazil and Mexico alone—but net bank exposure was up less than 2 percent in 1984 partly because of debt repayments and partly because some loans were written off as losses. [redacted] 25X1

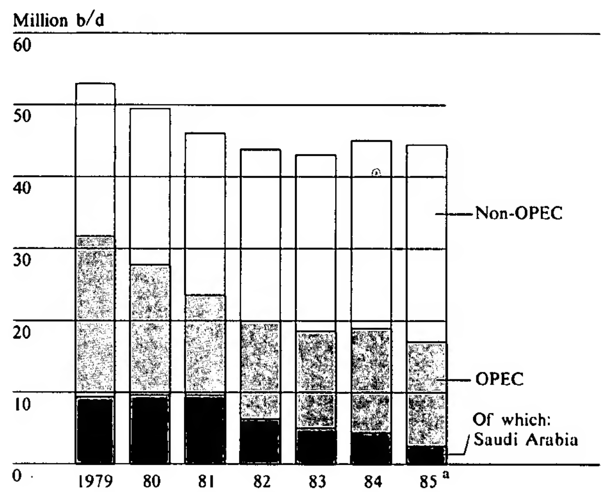
Over the near term, the activities of both borrowers and lenders in the international capital markets will be marked by caution. Commercial bankers will attempt to limit their exposure, even in those countries that have avoided debt servicing difficulties. At the same time, the developing countries that have accomplished some significant external payments adjustments will exercise borrowing restraint of their own. [redacted] 25X1

[redacted] 25X1

Medium-Term Oil Market Outlook [redacted]

OPEC will have a difficult time preventing a further drop in oil prices over the next 18 months. Prospects of continued weak oil consumption and rising non-OPEC supply availability will keep demand for OPEC oil at or below the group's current production ceiling. The key to preventing a major price decline is producer discipline. Thus far Saudi Arabia has borne the brunt of production cuts needed to maintain prices, but [redacted] it will no longer singlehandedly act as the organization's swing producer. Financial pressures will make it difficult for a number of OPEC countries to remain within their production quotas for any extended period. Downward price pressures could ease in the 1987-88 period if demand for OPEC oil rises, but ample capacity will keep market conditions soft. Although the impact of an oil price decline would generally be favorable for the world economy, a sharp fall in prices could require some economic and political adjustments. [redacted]

Non-Communist Oil Supply, 1979-85



a Estimated.

[redacted]

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Market Pressures Build

Weak oil demand, rising non-OPEC supplies, and substantial excess production capacity in OPEC countries are causing downward price pressure. Conservation and substitution kept non-Communist oil consumption in first-half 1985 about 1 percent below year-earlier levels and more than 500,000 b/d lower than most oil companies expected. At the same time, non-OPEC supply, which approximated 26.8 million b/d during first-half 1985, was up about 500,000 b/d from average 1984 levels. Weak demand pushed OPEC crude oil production down to 14.5 million b/d in June, including only 2.5 million b/d in Saudi Arabia. In an attempt to placate the Saudis and relieve market pressure on heavy crude prices, a majority of OPEC members agreed in July to reduce heavy crude prices by as much as 50 cents per barrel. Meanwhile, spot prices remain $1 to $2 per barrel below official levels. [redacted]

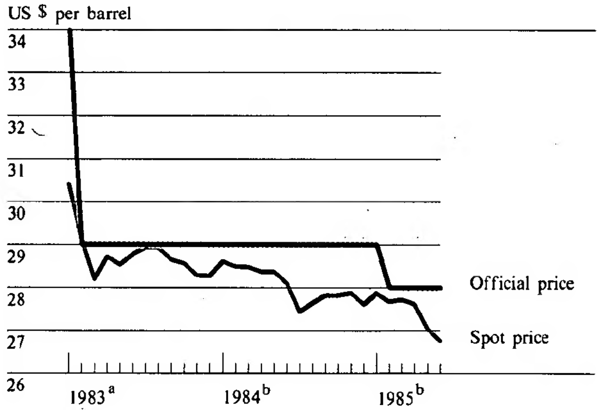
The Outlook for OPEC Through 1986

Non-Communist Consumption. We expect non-Communist oil consumption to register little or no increase and approximate 45 million b/d in both 1985 and 1986 in response to slower economic growth and continued conservation and substitution. Oil consumption in OECD countries as a group is expected to remain at or below 1984 levels

[redacted]

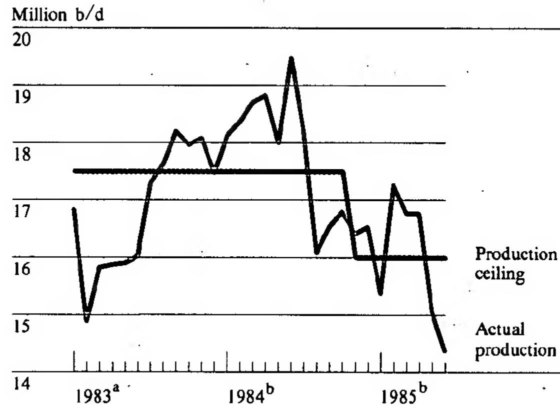
OPEC: Price and Production Trends, 1983-85

Arab Light Crude Prices



[a]1983:
February-March. OPEC agrees to reduce benchmark oil price $5 per barrel and set crude oil production ceiling of 17.5 million b/d.
[b]1984:
March-June. Iraqi-Iranian attacks on oil tankers keep demand for OPEC oil high.
July. Excess inventories, continued high OPEC production, and rumored Saudi barter deal cause sharp fall in spot prices.

Actual Crude Oil Production
Versus Production Ceiling



October. North Sea producers and Nigeria cut oil prices $1.35 to $2 per barrel; OPEC holds special ministerial meeting, cuts production ceiling to 16 million b/d.
December-January. After several false starts, OPEC agrees to realign differentials. Price of former benchmark crude, Arab Light, falls $1 per barrel. OPEC members also agree to retain an independent auditor to monitor members' production.

[redacted] 25X1

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in both 1985 and 1986 in response to continued substitution. Consumption in the LDCs is expected to rise by a few hundred thousand b/d in both years. [redacted] 25X1

Non-OPEC Oil Supplies. Industry forecasts project that non-OPEC oil production, including natural gas liquids and net Communist exports, will increase nearly 1 million b/d in 1985 to about 27.2 million b/d. About 500,000 b/d of this increase is expected to occur in the non-OPEC LDCs [redacted] 25X1 [redacted] 25X1 Brazil, Egypt, India, and Oman probably will account for approximately three-fourths of the increase in LDC output. Most industry forecasters estimate non-OPEC supplies in 1986 will increase by only about 500,000 b/d above 1985 levels. All of the increase in supply in 1986 is expected to occur in the developing nations, while OECD production holds relatively flat. [redacted] 25X1 [redacted] 25X1

Inventories. We estimate that primary oil stocks at the end of June 1985 stood at 4.0 billion barrels—the equivalent of about 92 days of consumption—and 100 million barrels above planned levels. Government-owned stocks account for about 600 million barrels of the total, or about 14 days' supply. Expectations of lower oil prices and continued belt-tightening by the oil industry suggest oil companies will attempt to pare excess inventories in 1985. We assume non-Communist oil stocks will decline by 600,000 b/d in 1985 and will hold steady in 1986. [redacted] 25X1

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Non-Communist Oil Demand and Supply Outlook *Million b/d*

	1984					1985					1986
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total	
Consumption	46.8	44.1	43.7	45.8	45.1	46.8	43.3	43.3	45.9	44.8	44.8
Inventory change	−1.3	2.0	0.6	−1.3	0	−2.3	0.4	0.2	−0.8	−0.6	0
Supply	45.5	46.1	44.3	44.5	45.1	44.5	43.7	43.5	45.1	44.2	44.8
OPEC	19.6	20.0	18.2	17.8	18.9	17.8	16.7	16.1	17.5	17.0	17.2
Non-OPEC	25.9	26.1	26.1	26.7	26.2	26.7	27.0	27.4	27.6	27.2	27.6

[redacted] 25X1

Demand for OPEC Oil. Given our estimates of consumption, non-OPEC oil production and inventory trends, demand for OPEC oil—including about 1.3 million b/d of natural gas liquids—will approximate only 17 million b/d in 1985 and 1986, causing demand for OPEC crude to remain at or below the organization's current 16 million b/d ceiling.[2] This forecast indicates revenue pressures on OPEC members will mount; we estimate that at current prices OPEC production would have to average about 21 million b/d in 1986 to prevent a further decline in the foreign exchange reserves of member countries. Moreover, demand for OPEC crude could fall substantially below the quota in response to seasonal changes in consumption. In addition, completion of Iraq's spur line to Saudi Arabia by early 1986 could add another 500,000 b/d to world oil supplies. [redacted] 25X1

Oil Price Scenarios

The world oil demand outlook suggests OPEC will have difficulty holding the line on prices. While predicting the magnitude and timing of possible oil price declines is difficult, we have looked at several possible scenarios:

- The organization's options for restoring *price stability* are limited, but OPEC could maintain nominal prices if Saudi Arabia continues its role as swing supplier and OPEC cohesion increases. Unless demand for OPEC oil rebounds in response to higher oil consumption, or lower non-OPEC supply availability, this scenario is unlikely.

- OPEC members continue to undermine the official price structure, forcing a series of minicrises and price cuts that allow a *controlled descent*. Saudi Arabia engineers several small price cuts that cause temporary periods of renewed OPEC discipline, but overall some members—Nigeria and Ecuador, for example—produce above ceiling levels and many producers discount oil as spot prices fall. Many industry sources expect this scenario to develop.

- A *price collapse* would result if OPEC's discipline breaks down completely. Under this scenario, widespread cheating by other OPEC members causes the Saudis to stop supporting prices. Riyadh gambles that a sharp price break will force greater producer cooperation and is needed to ensure a rebound in oil demand. The short-term revenue losses to other oil producers and the associated political impact on the Saudis, however, would be extremely costly. The probability of this scenario would increase if oil consumption trends downward. We are uncertain how far prices would fall in this case but some industry experts believe prices initially could fall well below $20 per barrel. [redacted] 25X1

[2] The OPEC ceiling does not include natural gas liquids. [redacted] 25X1

Market Prospects Beyond 1986

The outlook for oil prices in 1987 and 1988 will depend primarily on the way events unfold in 1985 and 1986. Under most circumstances we believe the market will remain soft and real oil prices will continue to fall. Assuming annual economic growth in the OECD averages 2.5 to 3.0 percent, non-Communist oil consumption is expected by most market forecasters to increase only slowly, perhaps by 1 percent annually or roughly 500,000 b/d. Conservation gains, increases in non-OPEC supplies, and substitution away from oil are expected to continue—albeit at a declining rate. Most industry forecasts expect non-OPEC supplies will peak during the period as expected declines in US production and in Communist oil exports offset increases in LDC production.

Under these conditions, demand for OPEC oil could increase slowly to perhaps about 18-19 million b/d by 1988 and help encourage producer cooperation. Nevertheless, we expect excess available capacity to keep market conditions soft through 1988 and cause a further erosion in real oil prices. A very sharp fall in nominal oil prices in 1985 or 1986 would hasten adjustments both in excess supply capacity and in demand by slowing substitution and conservation worldwide. 25X1

Implications

The impact of an oil price decline would generally be favorable. Lower prices would accelerate economic growth, dampen inflationary pressures, and reduce Soviet hard currency earnings. A price drop to $20 per barrel would improve the OECD trade balance by lowering the oil import bill by roughly $47 billion. Oil importing LDCs would benefit through lower import prices, higher demand for their exports, and lower interest rates. Respite from their financial burdens could improve prospects for political stability in some of these countries. 25X1

A sharp fall in oil prices, however, could create problems that would require some economic and political adjustments. Sharply lower oil prices could renew strains in the financial community as already indebted oil exporters endure new hardships. At $20 per barrel OPEC oil revenues would fall about $39 billion. Mexico, Nigeria, Egypt, Venezuela, and Indonesia would be especially hard hit given current financial problems. Development plans for some nonoil fuels would be postponed until the market stabilized, and pressure on banks with substantial energy-related loans could increase. In addition, development of North Sea natural gas could be delayed opening the door for greater Soviet penetration of the West European gas market in the 1990s. In the longer term, lower oil prices will slow conservation and substitution, hastening a return to a period of high industrial country dependence on insecure Persian Gulf oil supplies. 25X1
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Nicaragua: Coping With the Economic Crisis [redacted]

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The Sandinista leadership is now far more openly admitting Nicaragua's growing economic difficulties. Initiatives to stem declining living standards have been largely ineffective because the regime is unable or unwilling to address the main causes of the problem—increased military spending, mismanagement, and restriction of the private sector. Only a massive increase in aid from the Soviet Bloc is keeping the economy from collapsing but even this influx is only slowing, rather than reversing, the deterioration. [redacted]

Economic Deterioration

President Ortega has publicly acknowledged an inflation rate of 125 percent—we believe it is currently running at over 200 percent at an annual rate—and other officials admit that living standards have plummeted because of lagging wage increases. In 1985, wages have increased only about 80 percent. [redacted]

Ortega claims the military's share has risen from 25 percent to 40 percent within the past year. [redacted]

This diversion of resources from civilian industries is crippling the economy in key areas. We estimate that GDP fell 5 percent last year and continues to decline this year. Press reports indicate cotton planting is down 13 percent from 1984, largely because state prices are too low to encourage private growers. Dairy and meat production has dropped sharply. Better prices in neighboring countries have led to increased cattle smuggling. Nicaragua is now importing meat from the USSR. [redacted]

Haphazard Policy Initiatives

Efforts to resolve economic problems have been inconsistent. To cut the budget deficit, Managua eliminated consumer subsidies in February by raising official prices on most consumer items to their black-market price. Since then, subsidies have crept back into the official price structure. Managua has increased official staple prices only 75 percent, while average black-market prices have risen by 400 percent. Moreover, under the new super commissary system the number of state stores—virtually the only legal outlets for consumer goods—was reduced from 100 to three, driving more consumers to the black market. [redacted] 25X1

Inflationary wage increases during the past two years have moved the lower middle class and poor onto the tax rolls and increased the tax burden on others. The Finance Ministry in early July announced a plan to revise taxes that ostensibly lowers rates across the board and only marginally reduces total tax revenues. The new plan addresses 25X1 the bracket creep for the middle and upper classes by lowering their tax rates, but many others, even with very low incomes, are paying taxes for the first time. [redacted] 25X1

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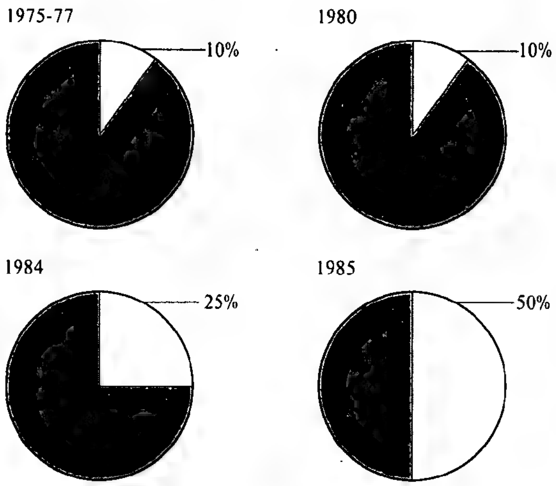
Agricultural Mismanagement

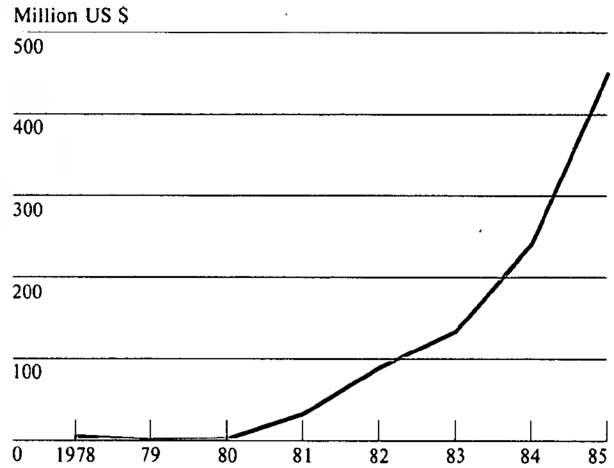
Managua continues to claim that it seeks a mixed economy, but its policies are driving independent landowners out of business. Private-sector sources estimate that since 1979 the Sandinistas have taken about two-thirds of the arable land. In mid-June Managua expropriated more than 3,600 hectares of productive farmland in the heavily populated department of Masaya and immediately distributed new land titles to peasant cooperatives, according to US Embassy reporting. Although Managua promised reimbursement, more than 1,200 hectares of rich coffee and cotton lands belonging to the president of Nicaragua's leading business association were confiscated without compensation. In 25X1

Nicaragua: Economic Indicators

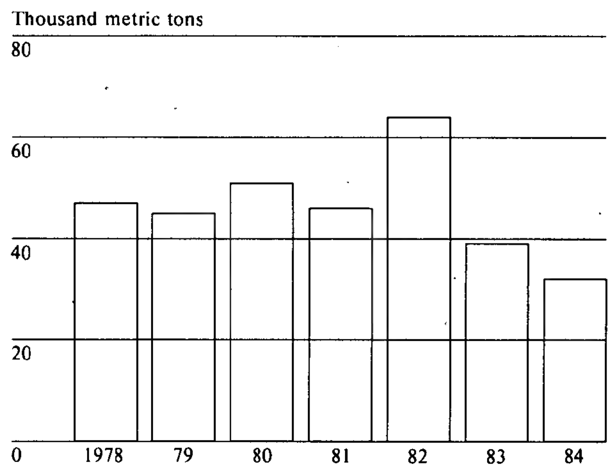
Military's Share of Total Budget



Imports From Soviet Bloc



Coffee Exports



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early August, the government expropriated 90 private farms to make room for an 11,800-hectare dairy project. The Sandinistas claim to be responding to legitimate demands for land reform, but the US Embassy reports that peasant demonstrations clearly have been organized by the regime and indicate that Managua may be preparing for further land seizures. [redacted] 25X1

US Embassy officials report recent Sandinista heavy-handed commercial regulations will seriously jeopardize Nicaragua's leading agricultural export—coffee. The government's purchasing authority arbitrarily discounted the weight of coffee beans by 20 percent to account for "water retention." Producers are countering by soaking their beans in water. At the same time, the state set a uniform price for all beans, regardless of quality. As a result, producers have even less incentive to bring to market high-quality, properly dried coffee, and the value of Nicaragua's coffee exports is almost certain to decline from last year's level. [redacted] 25X1

Soviet Aid

Only substantial increases in Soviet deliveries of petroleum, machinery, and consumer goods have averted the collapse of the Nicaraguan economy. In the first quarter of this year, imports from the USSR more than tripled over the same period in 1984, and the pace appears to be accelerating. [redacted] 25X1 Several East European countries have also supplied sizable amounts of foodstuffs and consumer goods. In addition, Moscow is also meeting almost all of Managua's petroleum requirements and continues to provide substantial supplies of military equipment. Cuba has been providing large quantities of items ranging from consumer goods to industrial machinery. [redacted] 25X1

Even though Moscow portrays the arrangements as purely commercial, cash-short Managua will be unable to make any substantial payments on its debts to the Bloc countries, and the Soviets probably do not expect to be repaid anytime soon. 25X1 Nonetheless, Soviet deliveries next year probably will stay at current levels and may even increase.

[redacted] 25X1

Indonesia: Attacking Domestic Inefficiencies

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President Soeharto is continuing his dramatic overhaul of Indonesia's inefficient economy in an effort to promote development of an internationally competitive manufacturing sector and reduce dependence on oil earnings. His latest moves—streamlining operations of Indonesia's notoriously inefficient ports and corrupt customs service—are aimed at slashing artificially inflated costs of imported materials for manufacturing industries. If these reforms take hold, they almost certainly will help domestic industries. We believe, however, Jakarta will eventually have to tackle reform of its tariff system to avert serious foreign payments problems later in the decade.

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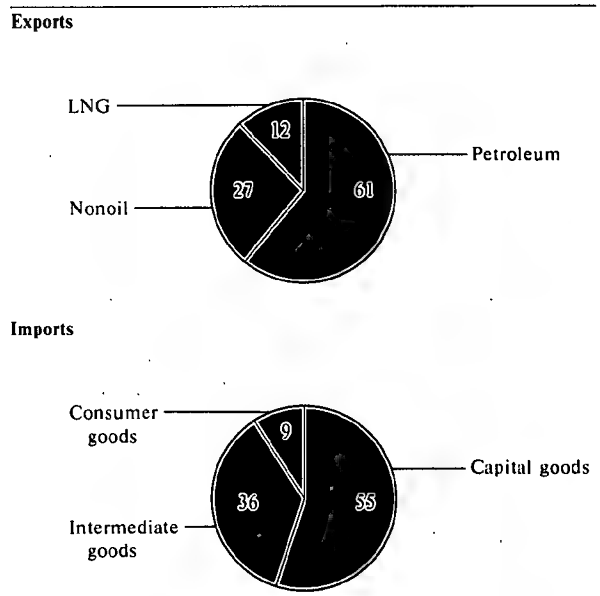
Indonesia: The Structure of Foreign Trade, 1984

Percent



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The Need for Reform

Indonesia traditionally has relied on petroleum and primary commodities rather than manufactured goods for its export earnings. Moreover, government efforts to foster import-substituting industries have led to an increasingly inefficient manufacturing sector dependent on protective trade barriers. Despite the sharp improvement in Indonesia's economic performance in 1984, this highly protectionist system has hobbled the international competitiveness of its manufacturing sector.

The present protectionist system includes tariffs on imports, quantitative restrictions, local content regulations, outright bans on imports of certain goods such as television sets, and licensing of importers. Bureaucratic ineptitude and corruption among well-placed officials have further increased the cost of imports and, since about 90 percent of Indonesia's imports consist of raw materials and intermediate goods, have weakened the competitiveness of export-oriented industries.

Artificially inflated costs are passed on to domestic industries by importers who control sources of supply. The World Bank has cited the impact of restrictions on steel imports, which are controlled by a few trading companies, as a special example. Although tariffs range only from 1 percent to 5 percent for most steel products, tight controls enable domestic producers to charge prices between 25 percent and 50 percent above world market prices. Among other things, this practice precludes the development of a competitive metal-fabricating industry.

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According to the US Embassy, subsistence farmers and consumers are among those seriously hurt by import controls. In a nation in which over 60 percent of the population is dependent on subsistence agriculture, a 50-percent duty and tight import controls have increased the price of a simple hoe to more than three times the world market price. A ban on television imports has led to the development of a television and electronics industry whose products cost 20 percent to 50 percent more than in international markets.

Targeting the Bureaucracy

Soeharto has not yet opted for wholesale dismantling of tariffs and quotas, but in a move as far-reaching as the austerity and reform measures [1] undertaken in 1983, Soeharto last April ordered a cleanup of Indonesia's ports and customs service. Long reputed to be the most corrupt element in the bureaucracy, the Customs Service has created a serious drag on the growth of the manufacturing sector. For example, an Indonesian businessman told US Embassy officials that 19 percent of shipping costs for rubber exports and up to 45 percent of port-clearing charges for machinery imports were "grease money" under the old system.

To reduce this burden on the economy, Soeharto has summarily relieved the Customs Service of most of its inspection functions and hired a Swiss firm to examine Indonesia's exports and imports. The government has placed about half of the 13,000 Customs employees on an indefinite furlough, which some observers believe is a predismissal leave. Soeharto has also suspended the previously required inspection of export shipments except for suspected contraband, taxable items, and certain other small shipments. The collection of import duties has been turned over to the foreign exchange banks. Harbor costs are to be reduced 50 percent through the rationalization of fees and the elimination of import monopolies.

[1] In 1983, Soeharto devalued the rupiah by 28 percent, drastically cut fuel and food subsidies, imposed budget austerity, and introduced major reforms in the banking sector designed to promote domestic saving and investment and tax reforms aimed at reducing the government's dependence on oil revenues.

Other Reform Measures

Jakarta is also proceeding with its program to streamline investment procedures. Potential investors have long complained of bureaucratic obstacles, duplicate and unnecessary paperwork, and excessive redtape. In the past year, Jakarta has eliminated a number of procedures and simplified others. In some cases, investors may apply directly for a final investment approval and avoid the previously required temporary approval, and they no longer have to supply invoices of the exact amount and value of machinery to be imported for a project. According to the US Embassy, Investment Board Chairman Ginandjar Kartasasmita recently said further changes are planned: new patent laws are being drafted, divestiture requirements for foreign investors are being reconsidered, and prohibitions on foreign participation in export projects will be eased.

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To ensure compliance with his order, Soeharto assigned Armed Forces Commander and Intelligence Chief Murdani to oversee port security—a veiled threat to opponents of the reforms that he would not tolerate opposition. Within a week of Soeharto's April decree, a package of 33 directives from the various ministries spelled out the new procedures and set time limits of three to seven weeks for implementing the system.

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The reforms initially gained a favorable response from shippers and manufacturers. The new regulations have cut port costs, slashed redtape, and reduced opportunities for illegal levies by customs officials. In the major Sumatran port of Belawan, for example, importers can now obtain their shipments with one signature, instead of the 36 previously required. Goods are clearing port more quickly, and turnaround time for oceangoing ships has

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been cut in half at an average saving of about $15,000 per day. Jakarta hopes that extreme cases, such as the instance revealed by an investigation of port operations in Surabaya in which goods had been held for 11 years, will be eliminated. [redacted]

Prospects

Soeharto's efforts to eliminate unnecessary regulations and reduce corruption almost certainly will help improve the competitiveness of domestic industry, but will require long-term presidential attention to produce lasting results. In the past, the government has made little more than cosmetic attempts to eliminate corruption. Soeharto is pursuing the current policies to make up for the expected impact of declining oil prices on Indonesia's earnings and will remain under stiff financial pressure to eliminate inefficiencies and obstacles to competitiveness for the next few years. [redacted]

While the measures undertaken so far are drastic by Indonesian standards, we believe further dramatic gains in cost reduction will be hard to achieve. Several key influence groups supporting Soeharto have benefited from the system and will resist efforts to undercut their favored position. In addition, there is a problem of corruption at the highest levels of government. [redacted] The brand new Sukarno-Hatta Airport in Jakarta, for example, is widely known among Indonesians as a financial fiefdom of the Soeharto family. [redacted]

Jakarta will have even more serious structural problems later in the decade if it leaves its protectionist foreign trade regime in place—a development that will intensify foreign payments problems. In the near term at least, the economy will remain heavily dependent on oil, a situation that will demand improvement in the competitiveness of nonoil sectors. By continuing to impose high costs on domestic manufacturing through tariffs on capital goods, however, Jakarta ensures that investment will continue to be diverted to inefficient enterprises serving the domestic market. This precludes a substantial investment in labor-intensive firms that might fuel more rapid nonoil export growth in the future. Unless and until Jakarta tackles the problem of tariff reform, we expect this investment pattern to continue to slow the growth of employment in manufacturing, and damage export competitiveness. [redacted]

[redacted]

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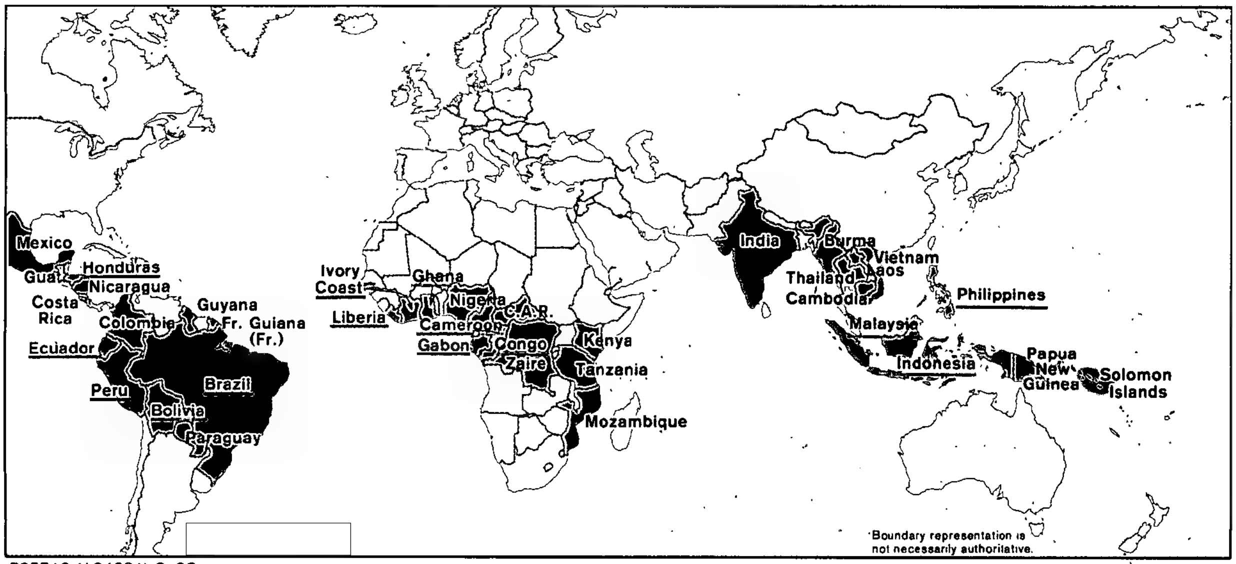
Countries Producing Tropical Timber

Country producing tropical timber whose timber resources are highly depleted

Country producing tropical timber whose timber resources have capacity for expanded exploitation

Malaysia Member of the International Tropical Timber Organization (ITTO)



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Tropical Timber: Intense Competition for a Declining Resource [redacted] 25X1

Intense competition among the leading timber exporters—Malaysia, Indonesia, and the Philippines—has created a depressed market for tropical wood characterized by restrictive trade practices, smuggling, and rapid resource depletion. Despite the current glut, the leading importers—Japan, the United States, and Western Europe—are likely to face serious tropical timber shortages and higher prices in the late 1980s or early 1990s. This price reversal could lead to greater substitution of domestically produced temperate hardwoods for tropical products as well as increased demand for US wood products in the lucrative Japanese market. In addition to pressures from the United States, Japan—the largest market for wood—faces increasing demands from Southeast Asian exporters for greater market access. [redacted] 25X1

Tropical Timber Agreement

The First International Tropical Timber Agreement entered into force 1 April 1985 following eight years of negotiations as part of UNCTAD's Integrated Commodities Program. Unlike agreements on coffee, sugar, tin, and rubber, the pact contains no provisions for controlling market supplies or stabilizing prices. Its objective is to provide a framework for cooperation between producing and consuming countries to promote expansion and diversification of trade in tropical timber. Only coffee and sugar among the nonoil commodities generate greater export earnings for LDCs than timber. The new agreement is unique in that it is the first pact to link trade with national policies aimed at conservation of resources. [redacted] 25X1

A Turbulent Tropical Timber Market

Malaysia, Indonesia, and the Philippines, which together account for about three-fourths of trade in tropical hardwoods, have become concerned about the viability of their timber industries. The big three producers have adopted policy measures—higher export tariffs and quotas, outright bans on log exports, and predatory pricing for wood products—that are reshaping trade patterns and spurring fratricidal competition. Moreover, the movement toward increased processing of logs into plywood and other wood products has created new tensions among the Southeast Asian producers. As a result of this intense competition in relatively weak markets, prices for logs, sawnwood, and plywood have fallen 25 to 35 percent from their peak levels in early 1980. [redacted] 25X1

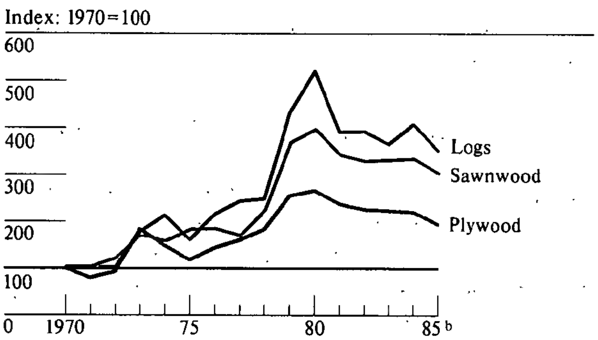
The Big Three Exporters—A Closer Look

Malaysia is the world's largest producer and exporter of tropical hardwood logs and lumber. Forest products are the mainstay of the economies of the East Malaysian states of Sabah and Sarawak and a major source of foreign exchange for Kuala Lumpur, $1.5 billion in 1984—10 percent of total export earnings. [redacted] 25X1

While the national forest-products sector is now experiencing a downturn due to soft demand and weak prices, there is growing concern over depletion of its timber resources. According to Kuala Lumpur, Peninsular Malaysia and Sabah could run out of commercial tropical forests by the end of the century or sooner. Peninsular Malaysia's forests are also under heavy pressure from slash and burn farming as well as large agricultural development schemes. [redacted] 25X1

Private-sector reforestation has been minimal because the cost is viewed as prohibitive given the long time span—50 to 70 years—required to produce a marketable stand. Kuala Lumpur is pushing

Selected Tropical Hardwood Prices, 1970-85[a]



[a] Average yearly price.
[b] January-June.

[redacted]

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reforestation programs, including the planting of new fast-growing softwood species, coupled with a reduction in logging rates to reverse what appears to be an inevitable decline in national output that is expected in the 1990s. The federal and state governments are also taking steps to encourage greater domestic processing of raw timber through log export quotas and bans and differential export taxes on logs versus products. Peninsular Malaysia banned all exports of tropical hardwood logs as of 1 January 1985. [redacted]

Indonesia, possessing the world's greatest remaining supply of commercial tropical hardwoods, has become the world's largest single exporter of tropical hardwood plywood. Tropical wood exports earned an estimated $1.1 billion in 1984, ranking only behind petroleum and natural gas exports. Of aggregate forest product exports, plywood accounted for 60 percent of total 1984 earnings or $667 million, more than double the level achieved in 1982. [redacted]

Jakarta's forestry policy seeks to substantially increase the value added of wood exports. In 1980, Jakarta began a policy of phasing down log exports, totally halting their export beginning this year. This policy has been tied to heavy investments in the processing sector estimated at over $2 billion over the last few years. Earlier this year, 10 new plywood plants were opened bringing to 96 the number of plants with a combined capacity of 4.7 million cubic meters annually. An additional 27 plants are now reportedly under construction. Current depressed demand for wood products and lack of access to the Japanese market, however, has forced some recent plant shutdowns. Moreover, in order to defend export prices, the government in May suspended export licenses of some plywood mills for undercutting fixed prices on sales to the US market. [redacted]

The Philippines ranks as the world's third-largest producer and exporter of tropical hardwoods. Increasing resource depletion, escalating costs, and heightened competition, however, have caused export earnings from wood products to dip to only 5 percent of total export earnings in 1984, from a peak of 25 percent in the late 1960s. [redacted]

The disappearance of the Philippine tropical forest resource base is particularly acute. According to a recent University of the Philippines study, mature tropical forest stands will be completely depleted before the year 2000, even if the rate of harvest declines. The study concludes, however, that if the annual timber drain continues at the rate of the past decade, tropical timber supplies from old growth forests could be exhausted as early as 1988. [redacted]

Manila's campaign against log smuggling appears to be fizzling out, according to US Embassy reporting. The heavy hand of the military is widely viewed to be a major problem for the industry. Military and Ministry of Defense officials own or control several lumber companies and use their power to the disadvantage of competitive private-sector firms. Legal operators are being forced to pay bribes to the Philippine Army and/or the New People's Army, and the smuggling of tropical logs overseas is rampant. According to press reports, an

Major Southeast Asian Tropical Hardwood Producers: Exports of Selected Hardwood Products, 1975-85 *Million Cubic Meters*

	Logs	Lumber	Plywood
Malaysia			
1975	10.79	1.91	0.23
1976	15.51	3.09	0.41
1977	16.12	2.99	0.34
1978	16.72	2.83	0.41
1979	16.50	3.54	0.47
1980	15.15	3.32	0.47
1981	15.87	2.81	0.47
1982	19.30	3.14	0.40
1983	18.81	3.49	0.48
1984	16.67	2.77	0.37
1985 [a]	15.50	3.00	0.30
Indonesia			
1975	12.88	0.40	NEGL
1976	18.11	0.66	NEGL
1977	18.93	0.59	NEGL
1978	19.46	0.76	0.01
1979	18.16	1.28	0.12
1980	15.18	1.21	0.25
1981	6.49	1.18	0.76
1982	3.22	1.24	1.23
1983	2.96	1.86	2.18
1984	1.73	1.45	3.02
1985 [a]	0	2.00	3.40
Philippines			
1975	4.60	0.25	0.16
1976	2.33	0.49	0.26
1977	2.05	0.46	0.34
1978	2.20	0.57	0.38
1979	1.25	0.92	0.42
1980	1.15	0.74	0.37
1981	1.68	0.55	0.40
1982	1.59	0.59	0.25
1983	1.02	0.73	0.30
1984	0.85	0.54	0.27
1985 [a]	0.37	0.35	0.18

[a] Estimated.

estimated $800 million worth of tropical logs were smuggled out in recent years, perhaps one-half the total to Japan. Advocates of a total log export ban believe it to be the only effective measure by which smuggling can be checked. Currently, the main policies to control log exports and encourage processing are differential export taxes on tropical logs and plywood. Tight credit and high interest rates have also discouraged much-needed investment. The Philippine Wood Producers Association has petitioned the government to place an additional 10-percent export tax on wood products earmarked for industrial tree plantations. 25X1

Trade Tensions Escalate

Tokyo's restrictive import policies—Japan accounts for roughly one-half of world tropical timber imports—are a major irritant to timber exporters. Malaysia, which continues to be the dominant supplier of tropical hardwood lumber to Japan, has also become Japan's largest tropical log supplier capturing 80 percent of the market. While there has been some growth in tropical hardwood plywood imports, the market is effectively blocked by Japan's high protective tariff. Southeast Asian countries, particularly Indonesia, are vigorously pressuring Tokyo to lower its duties on wood paneling—a symbolic issue in LDC complaints that Japan favors the United States and other Western countries. 25X1

Tokyo has promised to start a phasedown in its plywood tariff schedule beginning in 1987 as part of an as-yet-undefined restructuring of its domestic wood industry. While the prospect of greater market access is welcome news to US and Asian plywood exporters alike, Indonesia feels that this action will not be sufficient according to the US Embassy. With much of the plywood sector reportedly on the verge of bankruptcy, Jakarta believes that immediate access to the Japanese market is essential, and its wood paneling industry is considering placing a $20-per-cubic-meter subsidy on

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exports to the Japanese market. If enacted, Tokyo is likely to charge Indonesia with dumping to protect its large, politically powerful wood processing industry. [redacted] 25X1

Outlook and Implications

In the immediate future, importers should continue to benefit from soft prices. By the late 1980s or early 1990s, however, with the depletion of high-grade tropical hardwoods in key parts of Southeast Asia and West Africa, prices are likely to turn up sharply. This probably will spur logging in remote parts of Africa and the Amazon Basin, but costs of production are expected to be substantially higher than in more accessible traditional producing areas. Higher prices for tropical hardwoods are also expected to encourage major importers to substitute local woods—such as US temperate hardwoods, nonwood products, or other imported woods. [redacted] 25X1

In the huge Japanese wood import market, where growth in the use of domestic woods is not an important factor, increased prices, coupled with reduced availability of tropical logs for processing, could spur greater imports of substitute US temperate hardwoods as well as encourage the Japanese to find expanded uses for US softwood products. For both the United States and Southeast Asia, however, the level of access to Japan's wood paneling market will turn both on the tariff issue and on the tougher question of nontariff barriers such as standards and certification. The United States now faces a 15-percent tariff on plywood entering the Japanese market—the tariff on tropical hardwood plywood is around 19 percent. The long-sought-after tariff reduction plan for wood paneling recently announced by Tokyo as part of its Action Program for Improved Market Access could help to lift US solid wood exports; Japan is already the largest market for US forest products with sales

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Alternate Suppliers—Problems and Prospects

African countries for several years have supplied about 13 percent of the global volume of tropical hardwood trade with the Ivory Coast, Gabon, Cameroon, Liberia, and Congo the most important current exporters. Nigeria and Ghana, like Thailand, have been reduced to minor exporters in the last 20 years because of resource depletion. The Ivory Coast, which now supplies about one-half of African tropical log exports, is also confronted by decreasing production capacity due to resource depletion and lack of investment in the sector. In other countries, development of tropical timber exports still is handicapped by shortages in river, rail, and road infrastructure that add substantially to extraction costs. Another problem is that the greater diversity of African forests sometimes prevents local manufacturers from finding in any one species sufficient quantities to regularly supply importers over an extended period. As a result, only a handful of fairly abundant species dominate trade. [redacted]

Latin America's export flow only accounts for around 4 percent of current world trade, with Brazil being the only significant exporter. While the Brazilian Amazon accounts for 25 to 35 percent of the world's remaining stocks of tropical forests, their heightened exploitation presents significant economic and technical problems. While timber volume is immense—an estimated 260 million hectares in the Amazon Basin—tropical forest species composition is highly complex—even more so than in Africa. The result is that only a few commercially viable trees are potentially harvestable per hectare. In addition, extraction costs are further increased since much of the logging must be done manually in swampy seasonally flooded areas. Despite these constraints, Brasilia's goal is to make the country into the world's leading tropical timber exporter in the next 10 years. [redacted]

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of $1 billion annually. Reduction in Japanese tariffs, if accompanied by an easing of nontariff barriers, could also lead to increased exports from the United States and for tropical countries such as Indonesia, which have pinned much of their forest-sector export goals on increased access for value-added forest products. [redacted] 25X1

[redacted] 25X1

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Gulf Cooperation Council: Economic Integration Efforts

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The Gulf Cooperation Council (GCC),[1] which is embarking on its fifth year, has made progress toward its principal goal of increased cooperation among the member states. Although recent attention has focused on security coordination, most of the initiatives implemented to date have been in the economic sphere. The GCC has set the framework for economic and commercial ties, taken steps to link the infrastructures of the member states, and begun testing its powers as an international economic entity. Depressed oil revenues have, however, complicated the Council's already difficult task of implementing its ambitious aims. The GCC's efforts may have reached a plateau, because the relatively easy steps have been taken and those remaining will be harder to tackle; full economic unification is unlikely. 25X1

Agreement and Implementation

GCC members signed the Unified Economic Agreement in June 1981, which outlined broad goals for economic integration of the member states. These included: technical, financial, and monetary cooperation; the coordination of commercial and development policies, transport, and communication; and free movement of citizens and capital. 25X1

The first institution created by the GCC was the Gulf Investment Corporation (GIC). It was to be capitalized at $2.1 billion—paid-in capital totals only $420 million—with equal contributions by member states, and used to finance projects both within and outside the Gulf. A profit-oriented company, the GIC talks about investment in the GCC countries, but it has not invested in any GCC project. Rather, it has spread its investments abroad, acquiring equity interests in foreign companies with links to GCC states. In fact, allocating projects among the members has been difficult

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The Integration Concept

The GCC, created in May 1981, provided a multilateral institution based on already existing bilateral cooperation. In addition, it created a forum for the states to address their common interests and problems—all six are conservative governments with close ties to the West, whose societies are undergoing rapid changes financed by oil revenues, and who are concerned about protection against their more powerful neighbors. 25X1

The ultimate objective of the GCC was Gulf Arab unity, but the impetus for its creation was the outbreak of the Iran-Iraq war. Cooperation offered the regimes the best hope for survival in the face of threats to their security, particularly from Iran. Once the idea of regional cooperation was agreed upon, Gulf leaders saw advantages in economic cooperation because of their small populations and limited range of goods: 25X1

- *Economies of scale might permit the development of capital-intensive import substitution or export promotion projects. Products intended chiefly for domestic use would have a larger and more stable market, and large export projects could be financed.* 25X1
- *The elimination of custom tariffs would allow for freer movement of goods among the members.*
- *United action might make it possible for the Gulf states to obtain better terms from their trading partners.*
- *A regionwide program for developing infrastructure could increase efficiency and diversify the sources of income.* 25X1

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[1] The GCC comprises Saudi Arabia, Kuwait, Bahrain, Qatar, United Arab Emirates, and Oman. 25X1

because each state demands, for example, its own airline, steel mill, or cement factory.

In March 1983, a provision allowing GCC citizens to provide professional services, seek employment, and invest in other member states took effect. Commerce, real estate, and financial services—the major nonoil economic activities in these countries—are not covered, however. Investment by nonnationals is restricted to 25 percent of equity.

The first step toward a common external tariff policy was implemented in September 1983. The minimum tariff rate was set at 4 percent, although each state was allowed to draw up a list of foodstuffs and essential commodities that could enter duty free—48 percent of Saudi import categories, for example, are exempt from tariffs. Higher rates can be charged on some goods to protect local industries. Goods manufactured in a member state are exempt from tariffs if they meet agreed-upon criteria.

During 1984 the GCC implemented a series of policies designed to eliminate barriers to the free movement between member states of all factors of production. It issued unified passports to citizens of member states. Members of a variety of professions were permitted to practice in any of the GCC states. Real estate, if used for the residence of a GCC national, could be owned, with certain restrictions, in other member states. The Gulf Standards Organization was established, essentially replacing the Saudi Arabian Standards Organization. Joint procurement of pharmaceuticals, computers, veterinary medicines, and other commodities got under way. In addition, the cornerstone of the Arabian Gulf University—an institution open to students from all GCC countries—was laid in Bahrain.

The Greater Goals: Pipedreams?

Having successfully concluded several projects, including setting up its organizational framework, the GCC has begun to consider more grandiose undertakings. Among these are a GCC crude oil pipeline that would bypass the Strait of Hormuz, an integrated gas distribution system, and a strategic petroleum reserve. Several large industrial projects and an electrical grid are also under discussion. 25X1

Unified economic policies, such as monetary cooperation, development of a common currency, and harmonization of internal fuel prices are being considered. They have also met to discuss manpower problems in the Gulf and ways to control the flow of expatriate labor, as well as food, agricultural, and educational policies from a regional perspective. 25X1 25X1

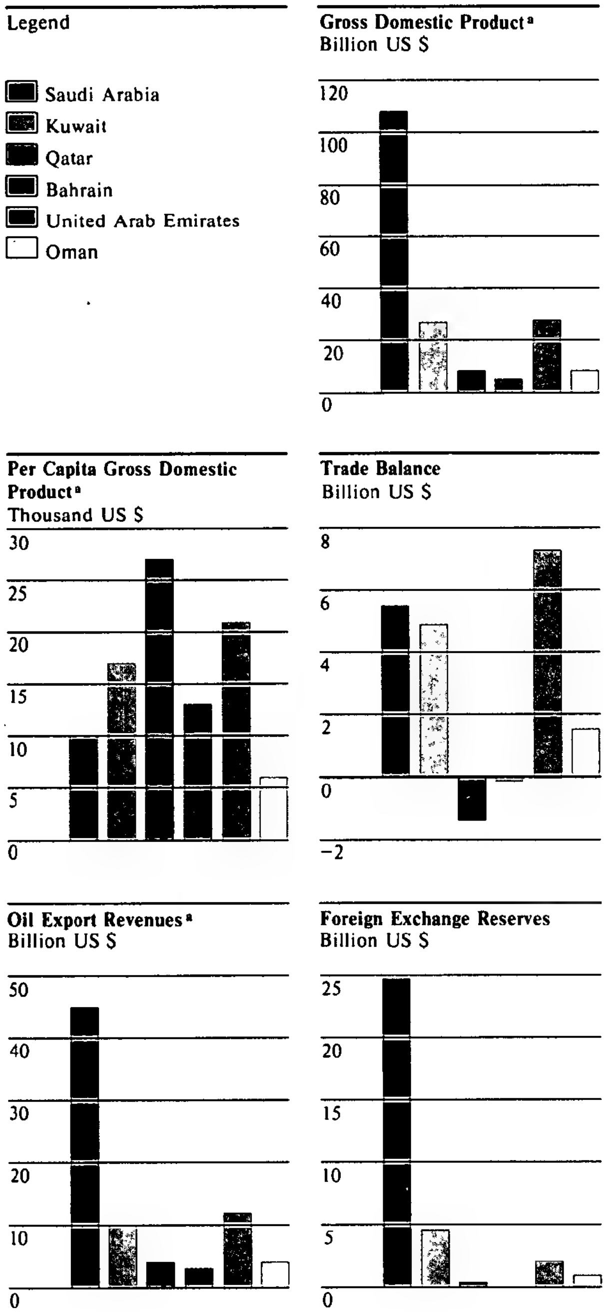
Many of the large infrastructure projects are too capital-intensive or complex to be implemented during a period of regional economic austerity. Member countries would find it difficult to justify large outlays for GCC projects at a time of domestic budget cutbacks, particularly if other members are perceived to be reaping the benefits. Moreover, goals such as monetary cooperation and a common currency require relinquishing control over economic policy, something the leaders are reluctant to do. 25X1

Changing conditions have rendered some GCC projects unnecessary. The gas grid project has been tabled because Kuwait has shifted to oil in previously gas-fed units, while Saudi Arabia has brought on nonassociated gas at a pace to satisfy all of its demand. Attacks on tankers in the Persian Gulf, which served as an impetus for the pipeline to bypass the Strait of Hormuz, has not disrupted oil shipments. 25X1

Prospects for Economic Integration

It is unlikely that the GCC will develop into a true economic unity, even if the oil market firms up. Although the member states have unified many aspects of their bureaucracies, trade, and commerce, they still act cautiously and agree only to 25X1 those initiatives that directly serve their interests. Converting broad goals into specific policies is difficult, and the task is complicated further because the Council's decisions must be ratified by all six heads of state. Moreover, there are so many loopholes and exceptions even in those policies—

Gulf Cooperation Council: Economic Indicators, 1984



[a] Estimated.

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especially regarding trade and commerce—that the policies often seem arbitrary and ineffective.

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Moreover, the smaller states are wary of Saudi ambitions, and their suspicions are likely to frustrate attempts at industrial, monetary, and developmental integration. These states look to the Saudis to provide leadership on political issues demanding Arab consensus, international economic issues, and defense. Still, they are worried about the potential for Saudi hegemony. The soft oil market and the dependence of each country on oil-based production also puts them in competition with one another. Considering the discounting and cheating on production quotas that the GCC OPEC members already engage in, harmonization of prices or production among GCC members would appear to be all but impossible.

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The Council has yet to grapple with the implications of continuing disparities in investment opportunities—stemming partly from tax and financing concessions and subsidies offered by the member states—or in income distribution. Nonetheless, the GCC has taken significant steps and is pleased with its progress to date. It has institutionalized the relationships of the six states, vastly improved regional communications, and encouraged closer cooperation. Although economic integration is still in the evolutionary stage, members are beginning to see themselves as a regional entity.

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Implications for the United States

The increasing convergence of views of the GCC states will require the United States to approach the GCC collectively on many issues. The GCC has approached the United States to propose exploratory trade discussions. The Council wants to discuss greater access to US markets for their petrochemical exports, joint ventures that would transfer technology, and liberalization of trade, perhaps leading to a free trade zone with the United States. 25X1 A GCC official recently cited relatively high US and EC tariffs, as well as the establishment of a US-Israeli free trade zone last year, as reasons for a similar trade arrangement.

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Briefs

Energy

OPEC Production Update

OPEC crude oil output in July averaged 14.7 million b/d, a slight increase from June levels. Oil market expectations of a possible cut in OPEC's official prices at its two July meetings kept production 1.3 million b/d below the organization's self-imposed ceiling. Saudi Arabia reportedly increased production to replenish floating stocks strategically located near major marketplaces. Higher Saudi output was offset by reduced production in Iran and Nigeria, both of which are looking to market their oil more aggressively.

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OPEC: Crude Oil Production, 1985 *Million b/d*

	Quota	First Quarter	Second Quarter	June	July
Total	**16.00**	**16.5**	**15.5**	**14.5**	**14.7**
Algeria	0.66	0.7	0.7	0.7	0.7
Ecuador	0.18	0.3	0.3	0.3	0.3
Gabon	0.14	0.2	0.2	0.2	0.2
Indonesia	1.19	1.3	1.1	1.0	1.0
Iran	2.30	2.2	2.6	2.3	2.2
Iraq	1.20	1.2	1.3	1.3	1.4
Kuwait [a]	0.90	1.2	1.0	1.0	1.0
Less share of Neutral Zone		0.9	0.8	0.8	0.8
Libya	0.99	1.0	1.1	1.1	1.1
Nigeria	1.30	1.6	1.4	1.2	1.0
Qatar	0.28	0.3	0.3	0.3	0.3
Saudi Arabia [a]	4.35	3.9	2.9	2.5	2.9
Less share of Neutral Zone		3.6	2.7	2.3	2.7
UAE	0.95	1.2	1.1	1.1	1.1
Venezuela	1.56	1.6	1.6	1.6	1.5

[a] Neutral Zone has no production quota; output is divided between Saudi Arabia and Kuwait and included in their country quotas.

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Reduced Oil Aid to Iraq

A source of the US Embassy in Kuwait reports that Neutral Zone oil sold on behalf of Iraq will be reduced from 248,000 b/d to 84,000-124,000 b/d. The Arabian Oil Company (AOC), which produces the oil and handles the aid payments for Saudi Arabia and Kuwait, had complained that the arrangement was causing them to lose money, and they would stop production unless given relief. AOC's contract calls for it to remit the cash equivalent of 248,000 b/d at official prices to Iraq. The slack market for heavy crude, however, has recently lowered AOC's sales to about 200,000 b/d, forcing them to make up the difference. The reduced flow of aid will cost Iraq at least $580 million over the next six months. This comes at a particularly bad time for Baghdad as it struggles to maintain finances through late this year when it starts receiving oil revenues from its new pipeline through Saudi Arabia. 25X1

Syrian Oil Developments

Syria's oil agreement with Iran for 1985/86 was recently approved by Iran's Consultative Assembly. The agreement again calls for Iran to provide Syria with 7.4 million barrels of free oil and up to 37 million barrels of oil at a $2.50 per barrel discount. The free oil plus the discount provides about $300 million in aid to Syria. Unlike the previous two contract years, Iran did not forgive or reschedule Syrian oil debts and the Assembly stated that all bills must be paid by 2 October 1985. Domestically, Syria has increased production from its new Thayyem oilfield in eastern Syria from 5,000 b/d to 12,000 b/d. The oil is being pumped through an unused gas pipeline to the Iraq-Syria pipeline and then on to the Homs refinery. Production at the field is now at the limit of the installed gas separation facilities at Thayyem. 25X1

Algerian-Yugoslavian Natural Gas Contract

Algiers and Belgrade signed an agreement on 30 July calling for the delivery of 20 billion cubic meters (bcm) of Algerian gas over 20 years beginning in 1988. Yugoslavia may have been attracted to the deal by the Algerian offer to help construct pipeline facilities at Arzew. Yugoslavia currently consumes about 6 bcm of gas annually—about 10 percent of its total energy requirements—with 3.7 bcm imported from the Soviet Union. The gas price is as yet unknown, but is expected to be equal to the price Italy pays for Algerian gas—about $3.50 per million Btu—with a discount for the higher transport cost. Delivery will require the connection at Genoa of the pipeline linking Algeria and Italy to the Yugoslav gas network. This agreement, together with the recent Algerian-Brazilian gas contract, marks a significant geographic expansion in Algerian gas marketing efforts. It also suggests Belgrade's willingness to diversify its sources of gas imports. 25X1

International Finance

Support for Peru's Ceiling on Interest Payments

President Garcia is likely to receive considerable tacit support from Latin American leaders for limiting debt repayments to 10 percent of export earnings over the next 12 months, but the support is unlikely to produce an overt bandwagon effect any time soon. Brazil's Foreign Minister Setubal

commended Peru for being the first Latin country to link trade and debt payments. [redacted] 25X1

Press reports indicate that Uruguay is studying a similar ceiling set at 20 percent of export earnings. In contrast, Argentine Foreign Minister Caputo has told US Embassy officials that Buenos Aires is displeased by Garcia's announcement because it weakens Alfonsin's standing at home and will create new political pressures for Alfonsin to adopt a hard line. [redacted] 25X1

Garcia's declaration generally is viewed as a radical action and, with several loans and reschedulings for Latin America now pending, he is unlikely to obtain broad regional endorsement. Some countries, however, may join Brazil in issuing sympathetic statements to intensify pressure on creditors for financial concessions. His proposal, however, could provide a rallying point for the region's debtors in the future, particularly if industrial countries enact new protectionist legislation. [redacted] 25X1

Costa Rican Financial Program in Trouble

Preelection politicking is complicating Costa Rica's delicately balanced financial stabilization program—the most successful in Central America—and probably will slow economic growth for the rest of the year. The US Embassy reports that San Jose failed the IMF's standby loan review last month, largely because opposition politicians have blocked approval of a World Bank loan. The action caused a $10 million drawing from the IMF to be suspended and a $40 million World Bank disbursement to be delayed. Moreover, nearly $60 million promised from commercial banks as part of the stabilization program are being held up. As a result, Costa Rican foreign reserves have plummeted, and creditors have been informed that they will have to wait longer for past-due interest payments. President Monge may be forced to strike a deal that gives opposition leaders much of what they want. Getting back into the good graces of the IMF and remaining in compliance for the rest of the year, however, will require tough measures to restrain government spending and to reduce imports and consumption further. The economy—which had rebounded by 6 percent in 1984—began to slow during the first half of this year. A major drop in banana production was chief among export problems. Economic growth for 1985 probably will be only 2 to 3 percent—not enough to increase real consumption levels. [redacted] 25X1

Nigeria's Mounting Financial Woes

A major international bank's decision to reduce trade credits to Nigeria by over one-third could trigger similar action by other banks and leave Lagos vulnerable to a short-term credit crisis [redacted] 25X1
[redacted] The US Embassy reports that local bankers are concerned that repayment delays on trade credits could prompt further cutoffs by foreign lenders. The country's already fragile cash-flow position had been weakened by a recent one-third decline in oil exports. The prospect of a significant reduction in trade credits may encourage Head of State Buhari to reach an 25X1

agreement with the IMF, which would provide access to about $3 billion in IMF and World Bank funds. The US Embassy reports Buhari took a more flexible stand toward the IMF in a recent radio interview. His weak political position, however, probably will make it difficult to implement risky IMF-sponsored reforms that could provoke serious public unrest. [redacted] 25X1

Guinea Prepares for IMF Agreement

The Guinean Government is taking steps to implement economic reforms under an IMF standby agreement. Conakry recently signed a protocol to establish an affiliate of a French bank in Guinea that will serve as the country's primary commercial credit institution. Guinea also has initiated a census of government workers as the first step toward reducing civil service and parastatal payrolls. These moves will facilitate final IMF standby negotiations set for October. [redacted] 25X1

[redacted] 25X1

OECD Nuclear Power Plant Financing Agreement

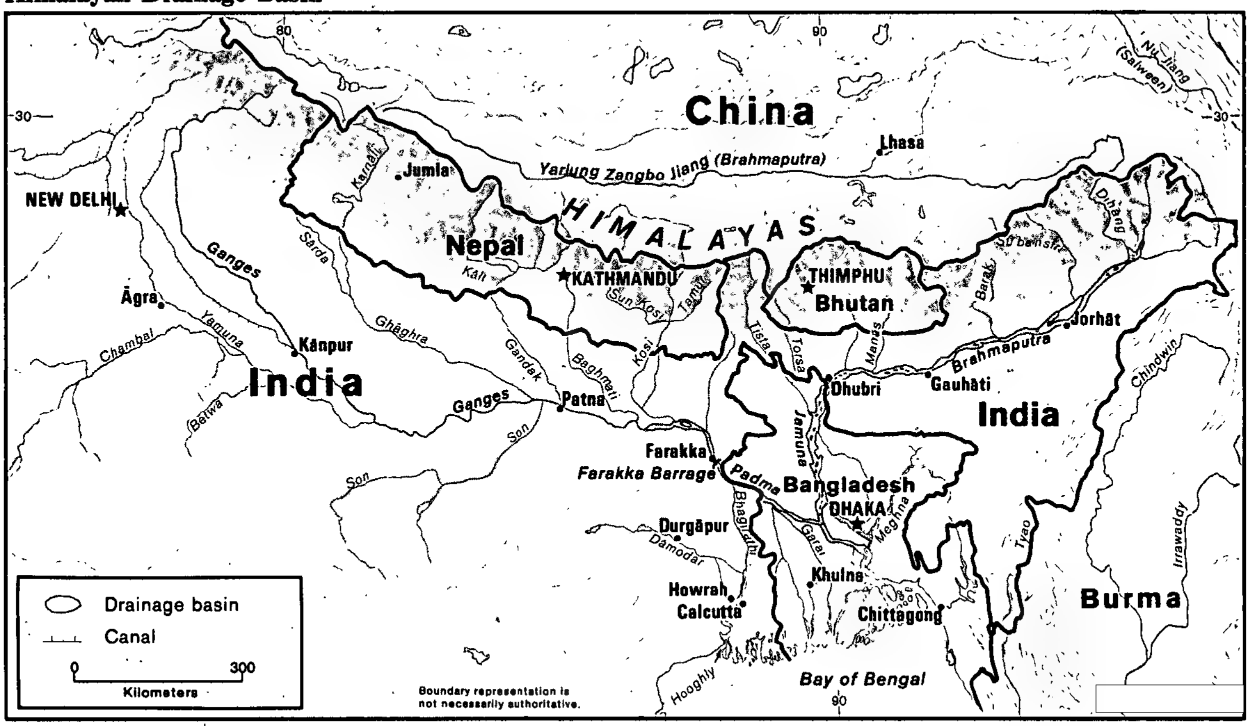
A potential delay has been avoided for the implementation of the interest rate provisions for the August 1984 OECD Nuclear Power Plant Financing Understanding, according to US officials. The new interest rate requirements were to go into effect 10 August 1985. Difficulties center upon how to establish minimum interest rates, known as special commercial interest reference rates (SCIRRs), for low currencies such as the yen. The EC, Canada, and the United States suggested a minimum interim flat rate of 8.1 percent, 0.5 percentage points above Tokyo's proposed SCIRR rate. Last month, a MITI official requested either US approval of Tokyo's proposal or delayed implementation of the interest rate requirements. Washington, however, maintained that waiting for overall agreement on SCIRRs would give other participants an excuse for failing to apply the provisions of the Understanding. As a result of US efforts, Japan agreed last week to an interim rate of 7.8 percent until the end of September. The yen SCIRR proposal will be discussed at the OECD Export Credit Group meeting in September. Although no major nuclear power plant contracts have been awarded since the Understanding was enacted, competition is especially keen for China's planned $5-6 billion investment in nuclear power over the next five years. [redacted] 25X1

Global and Regional Developments

Movement on Himalayan Water Sharing

In a surprising move, New Delhi has shifted its position on the longstanding water-sharing issue between India and Bangladesh [redacted] 25X1
[redacted] India's new position is a positive first step toward an integrated approach—long advocated by Bangladesh—to solving the water control problems of the Himalayan Basin. India is prepared to approach Kathmandu about constructing reservoirs in Nepal to store runoff from the Himalayas in order to augment the Ganges during the critical dry season. In the meantime, New Delhi reportedly has decided to extend the 1982 water-sharing agreement with Dhaka for another three years. Financial, technological, and political constraints, however, will make negotiations toward a tripartite agreement on water sharing difficult. [redacted] 25X1

Himalayan Drainage Basin



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EC Subsidizes Beef Exports to Asia

The EC has for the first time authorized subsidies for beef exports to Burma, China, Hong Kong, Indonesia, North Korea, Pakistan, the Philippines, Sri Lanka, Thailand, and Vietnam. The Community in February signed an agreement with Australia not to subsidize beef sales to Japan, Malaysia, Singapore, South Korea, and Taiwan. Although Australian beef exports to the 10 countries are limited, Australia, fearing further encroachment on its markets, officially protested the subsidies, but the EC is unlikely to be deterred. The Community is working to develop new export markets for its growing beef surplus. The surplus is, in part, the result of the slaughtering of dairy cows in the wake of last year's tightened quotas on EC milk production, and EC officials expect the surplus to diminish later this year as dairy herds stabilize at lower levels. [redacted] 25X1

Persian Gulf–EC Trade Dispute

Saudi press reports indicate that the Gulf Cooperation Council is considering raising its tariffs on West European goods in retaliation for tariffs on Saudi petrochemical exports. A final decision is expected this fall when the Council's Foreign Ministers meet. Exploratory talks with the Community, which Saudi Arabia hoped would lead to resolution of the petrochemicals issue and to an economic cooperation agreement, appear to have stalled, according to the US Embassy in Riyadh. The Europeans are concerned that competition from the Persian Gulf will adversely affect their declining petrochemical industries and are unlikely to react unless the Saudis actually impose tariffs. The Council is also seeking discussions on this issue with the United States probably reflecting Saudi concern about protectionist legislation that could curb Saudi petrochemical exports as well as disappointment with the Council's negotiations with the EC. [redacted] 25X1

Libyan-Italian Trade Talks End

Tripoli and Rome moved closer to resolving Libya's $600 million in commercial arrears and opened discussion on $1.5 billion in new contracts during the recent meeting of the Libyan-Italian mixed commission. Under the new agreement, Libya will continue to supply crude oil to Italy over the next year to cover $300 million in delayed payments on major projects and probably will ship additional oil to resolve $260 million in commercial arrears. In addition, the two parties probably will sign soon a long-term LNG contract for 1 billion cubic meters annually. Despite often acrimonious relations, both sides receive considerable benefits from their trade relationship. Libya meets 16 percent of Rome's crude oil needs and Italy remains Tripoli's largest source of imports—$1.7 billion last year. [redacted] 25X1

25X1

[redacted]

25X1

National Developments

Developed Countries

Canada To Control Foreign Investment in Publishing

Ottawa recently adopted strict new controls on foreign investment in publishing that will undercut its public relations campaign to attract capital from abroad. The new policy is intended to Canadianize the "culturally sensitive" industry, which is currently 80 percent foreign-owned. The program was announced by Minister of Communications Masse just six days after the inauguration of Investment Canada, a new federal agency to promote investment in Canada. Under the new regulations, foreign acquisition of existing publishing firms will only be authorized if the purchaser agrees to divest control to Canadians within two years. The new restrictions may affect several pending investment applications, the largest being Gulf and Western's indirect acquisition of Prentice-Hall Canada via its purchase of the US parent firm. The controls probably will be popular politically, but may complicate relations with trading partners, who are likely to object to the limits on indirect acquisitions as extraterritorial extensions of Canadian law.

25X1

Toyota To Export Cars from Canada

Toyota—which is planning to build automobiles in Canada beginning in 1988—may be designated a "qualified manufacturer" under the Canadian-US Auto Pact, thus permitting it to ship automobiles and auto parts duty free to the United States. Ottawa's ruling will be contingent on Toyota fulfilling two criteria. First, the value of cars produced in Canada must equal at least 75 percent of the value of autos it sells there. Toyota sold 49,463 cars in Canada in 1984, and 26,832 in the first half of 1985. The Canadian plant is scheduled to produce 50,000 of the less expensive Corolla models. Second, Toyota must purchase Canadian-made auto parts equal to 60 percent of the value of its Canadian sales. Its recently opened aluminum-wheel plant in British Columbia will help Toyota reach this level. Toyota will also use these parts to help fulfill the sole US requirement under the auto pact—that each car possess 50-percent North American content.

25X1

[redacted]

25X1

Japanese Unions Support Trade Liberalization

High-level union officials, traditionally quiet on trade issues, are now urging Tokyo to take additional steps to ease trade friction with the United States. In his capacity as representative of Domei, a major labor organization, and Zenmin Rokyo, an informal national council representing private-sector unions, Japanese Autoworker President Shioji recently appealed to officials at the Trade and Agriculture Ministries to liberalize Japan's markets. At the June meeting of the International Federation of Metalworkers, Japanese Steelworker President Nakamura stated his union's support for the elimination of remaining tariff and nontariff barriers and for domestic demand-led economic growth. Labor officials are probably concerned that growing domestic pressures on Washington to restrict imports from Japan would affect jobs in industries heavily dependent in exports. [redacted] 25X1

Japan's Labor Unions Eye Unification

Several recent events suggest prospects for unification of Japan's private-sector unions under a formal national center, Zenmin Rokyo, are improving. Established as an informal working group in 1982 by the four major national labor organizations, Zenmin Rokyo has been plagued by bitter political and organizational divisions. Last month, however, Churitsuroren, the third-largest labor federation, agreed to join the International Confederation of Free Trade Union (ICFTU), a precondition to Zenmin Rokyo membership. In addition, Ichiro Shioji, president of the powerful Nissan Autoworkers, may take over Zenmin Rokyo's top position. Leftist public-sector unions—critics of both Zenmin Rokyo and the ICFTU—expressed concern at the July Sohyo convention that a strong private-sector union organization will damage their interests. Unification of the private-sector unions could reinvigorate the annual spring wage offensive, which has not achieved targeted wage hikes in recent years. It also could help labor bargain for legislation for a shorter workweek. [redacted] 25X1

West German Labor-Government-Business Discussions

The Kohl government and the West German Trade Union Confederatioin recently announced they will hold tripartite talks on unemployment with business leaders this September, the first meeting of its kind since 1977. The cabinet and union leaders said they already are in agreement on the need to reform job training programs and old-age pensions, but Bonn has rejected labor's call for a new DM 50 billion ($17.5 billion) job-creation program. Although the agreement on the meeting is a political plus for Kohl, the unions still are planning nationwide demonstrations this October against his austerity measures. They probably are trying to demonstrate moderation to the public and gain some leverage with the government. Moreover, labor-government relations may worsen sharply if Kohl follows through with plans to introduce legislation weakening the unions' powers in contract negotiations. [redacted] 25X1

Spain Postpones Labor Reform

To win trade union acquiescense on a social security reform bill, Madrid has agreed to back off, at least temporarily, on its plan to free up Spain's rigid labor market. The Socialist government has pushed pension reform to slow the soaring costs of the state-supported social security system, and at the same time has pressed to relax the stringent regulations on company layoffs and dismissals—which boost labor costs and helped contribute to the 22-percent unemployment rate. The General Workers' Union, the labor arm of the ruling Socialist Party, came out against both measures, because of increased worker contributions to the pension system and fears of higher unemployment due to easier layoffs. Because high labor costs are largely responsible for current sluggish investment, the compromise is certain to hinder Spain's overall reindustrialization plan and economic austerity program. Despite protests from the business community, however, we believe the government will hold off on labor reform until after the national elections next summer. [redacted] 25X1

Less Developed Countries

Mexican Prospects for Reducing Deficit Bleak

Recent government projections indicate that economic measures announced late last month will not significantly trim government spending. [redacted] 25X1
[redacted] government analysts forecast a budget deficit equal to 9 25X1
percent of GDP. Meanwhile, [redacted] international 25X1
bankers believe the negligible impact of the measures to cut the budget increases the likelihood that Mexico City will seek a new round of debt rescheduling talks early next year. The deficit figure is far above the 4.9 percent agreed to with the IMF in March. The Fund is aware Mexico is having difficulty meeting its fiscal targets, and any release to the public of such a large estimate of the deficit would make negotiations scheduled for September even more difficult. [redacted] 25X1

Mexico Considering Entry Into GATT

The Mexican Government appears to be seriously considering membership in GATT, according to the US Embassy, although in the past it has been reluctant to take this step. Commerce Secretary Hernandez last week told

reporters that Mexico may join GATT if members offer unspecified major concessions in response to recent Mexican trade initiatives. If fully implemented, recent import liberalization measures would bring Mexico closer to GATT practices. Entry into GATT, however, would be politically difficult for President de la Madrid, and the undefined concessions required by Mexico are likely to be a sticking point. Opposition to joining GATT is widespread, encompassing the private sector, which favors continued protectionism, and leftists, who view GATT membership as a threat to Mexican sovereignty. The government's latest trial balloon may be intended mainly to placate international financiers, who are increasingly worried about the Mexican economy. [redacted] 25X1

Chilean Efforts to Develop Southern Region

Santiago, with the aid of international investors, is taking steps to develop its resource-rich southern region, but geographic constraints and a sagging economy are likely to make profitable exploitation difficult. Chile recently received a loan to develop the Pecket coal deposit near Punta Arenas and to build a port for shipping coal north to the state-owned copper company, CODELCO. Other projects under way include a methanol plant and a fertilizer plant, both of which will take advantage of abundant natural gas reserves, and there are plans to improve the port facilities at Punta Arenas and the highway network throughout the far south. The Magellanes region contains all of Chile's known reserves of 250 million barrels of oil and 1.9 trillion cubic feet of natural gas, and most of its 6 billion metric tons of coal. Magellanes, however, is cut off from the heavily populated central region by a jagged coast, mountains, icefields, and glaciers, and no highways connect the south to the rest of the country, necessitating heavy reliance on seaports and expensive air transport. [redacted] 25X1

Moroccan Austerity Prompting Dissident Activity

Morocco's deteriorating economy and the ostentatious lifestyles of the elite—including the King—are fueling demands for change from Islamic fundamentalists and other opposition elements. Residents temporarily displaced by the expansion of King Hassan's palace in Casablanca took to the streets late last month to demand restitution. Two thousand police were brought in to restore order after a local flour mill was burned and Islamic slogans criticizing the King appeared on walls near the palace [redacted] 25X1 Moreover, military security in Casablanca believes that enlisted personnel are being actively cultivated by Islamic groups. The activism of Islamic organizations has paralleled Morocco's economic decline, and we believe that Islamic fundamentalism will increasingly provide a vehicle for expressing the frustrations of the disadvantaged and disaffected. [redacted] 25X1

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Sudan Adopts Currency Reforms

Sudan's Ministerial Economic Council has moved to restore order in the chaotic foreign exchange market by pegging the pound to a currency basket set forth in recent negotiations with the IMF, according to the US Embassy. The new system conveniently circumvents Sudanese law that requires presidential approval of any devaluation. Moreover, the system of weekly adjustments in pegged rates permits gradual devaluation by the Bank of Sudan without the publicity and upheaval associated with past currency adjustments. The currency compromise also clears the way for new negotiations on an IMF program scheduled for September. Government officials believe that official and black-market exchange rates will initially converge at 3.7 pounds per US dollar. The swift movement on currency reforms underscores the influence of the Finance Minister who has emerged from the recent resignation episode with an even stronger hold on economic policy. His adept handling of the touchy devaluation issue shows a marked improvement in Sudan's financial planning and should limit criticism from powerful labor and opposition parties. [redacted] 25X1

Zimbabwean Budget

The fiscal year 1985/86 budget introduced earlier this month features a substantial increase in deficit spending that is likely to complicate negotiations for a new IMF standby agreement. Expenditures are set to rise by 18 percent, compared to a prevailing 10-percent inflation rate. Revenues are projected to increase by 15 percent, primarily on the strength of export earnings and higher foreign aid. The $512 million deficit is equal to about 11 percent of projected GDP, which is well above the 5.5-percent target in the last IMF agreement. Much of the planned increase in expenditures are to cover aircraft purchases and military support for neighboring Mozambique. [redacted] 25X1

Islamabad's Bond Sales Slower Than Expected

Sales to date of special national fund bonds, designed to attract funds from the black market, have been slow in spite of strong government exhortations. [redacted] the government—which had 25X1 hoped to raise 3 billion rupees ($190 million) to partially offset budget deficits—is unlikely to raise more than Rs 1.5 billion ($95 million). Banking officials report several reasons for slow sales including interest rates lower than those available elsewhere and expectations that, in the face of slow sales, the government will shortly increase returns on the bonds. Even with a spurt at the 31 August deadline for purchases, sales probably will remain well below official goals. The poor sales performance of this first issue suggests that Islamabad will have to look for alternate means of deficit financing, most likely increased borrowing from domestic banks. Pakistan probably will also reduce spending on social programs. [redacted] 25X1

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Communist

New Economic Experiment in Soviet Industry

A managerial reorganization program—described as a model for the rest of the economy—is under way at the Ministry of Instrument Manufacturing (Minpribor), according to recent Soviet press reports. The program includes reducing the number of plan indicators used to evaluate enterprise performance, eliminating the management level that lies between the enterprise and Ministry, and creating additional scientific production associations to spur R&D and prototype production. The Minpribor program, which aims at streamlining an industry critical to Soviet technological progress, is a reflection of the moderate nature of the innovations Gorbachev is pushing. Most, if not all, of its elements have been tried before. Reducing the number of plan indicators and expanding the use of scientific-production associations have been regime goals for more than a decade. While the experiment will eliminate an entire middle layer of bureaucracy, 85 percent of the affected personnel are being transferred to the central ministry, presumably to do much the same jobs. [redacted] 25X1

[redacted]

25X1

USSR Orders East German Ships

The Soviet Union has ordered 16 new Astrakhan class, combination-loading merchant ships from East Germany. The new ships are equipped with vehicle-loading ramps and heavy-lift deck gear enabling them to discharge cargo in Third World ports without dock facilities. Like traditional break-bulk ships, they have separated holds and large hatches that can carry a variety of cargo, including dangerous cargoes such as ammunition and, with the heavy-lift gear, heavy cargoes—like aircraft crates. These ships also carry standard shipping containers. The Soviets have received six of the 16 ordered and have been using five for commercial cargoes and one for transporting arms to the Third World. Because of their versatility, we expect to see more of these ships used as arms carriers. [redacted] 25X1

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Poland's 1986-90 Economic Plan

The 1986-90 draft economic plan adopted by the Polish parliament in late July projects moderate growth in national income and investment, a slight increase in consumption, but makes no commitment on the question of economic reform. National income growth projections of 3.5 percent annually, if achieved, would bring the level of output in 1990 almost back to its 1978 peak. The growth projection, however, lacks specific policies about how to improve the use of capital, labor, energy, and raw materials, and is generally overly optimistic. The plan also gives priority to the completion of outdated investment projects that are unlikely to bring sustained growth in production. Increased investment is needed to halt the aging of Poland's capital stock and to modernize Poland's export industries. Although increases in consumption are slated at 1.8 percent annually, the regime is likely to give in—as in the past—to pressure for greater consumer outlays. The official trade unions have already pointed out that increased housing construction, better health care, and improvements in environmental and working conditions would reduce social tensions and boost labor productivity. 25X1

Polish Economic Performance: 1984 and 1986-90 Plan

Average annual percent

	1986-90 Draft Plan	1984 Actual
National income	3.5	5.0
Investment (total)	5.9	8.0
Per capita consumption	1.8	4.0
Real wages	1.8	3.1
Exports	6.1	9.0
Imports	4.9	9.0

25X1

Problems Delay Bulgarian Recovery

The Bulgarian economy is still struggling with dislocations caused by harsh weather last winter. In late July the regime reinstated household electricity rationing first imposed last winter. [redacted] Bulgaria has been buying coal and oil on international markets because Soviet supplies are lower than in previous years. Insufficient rainfall this year has curtailed hydroelectric generation and irrigation and forced Sofia to impose strict water conservation measures. Drought and winterkill have hurt this year's grain production. Bulgaria, usually a net wheat exporter, is reportedly trying to purchase grain from Argentina and China, and the government has urged reduced consumption of foodstuffs, especially bread. According to official data, the energy, metallurgy, chemical, and construction industries were short of planned targets for the first half of the year. Although bad weather was cited as a factor, the problem was complicated by waste, management errors, poor worker discipline, and lack of technological know-how. Measures to increase production—including a compulsory six-day workweek since April and exhortations to work harder—may be having some effect. A regime report in early August noted a "steady trend toward improvement." [redacted]

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Directorate of
Intelligence

Economic & Energy Indicators

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Industrial Production

Percent change from previous period seasonally adjusted at an annual rate

	1981	1982	1983	1984	1985					
					1st Qtr	2d Qtr	Mar	Apr	May	Jun
United States	2.6	−7.2	5.9	11.6	2.1	2.2	2.9	2.9	1.0	1.9
Japan	1.0	0.4	3.5	11.1	−2.6	12.5	−15.7	39.0	32.6	−13.5
West Germany	−2.3	−3.2	0.3	2.4	−4.6		15.6	18.2	−15.4	
France	−2.6	−1.5	1.1	2.6	−3.0		19.8	−23.8	19.9	
United Kingdom	−3.9	2.1	3.9	1.2	8.7	8.9	18.6	13.1	6.9	6.5
Italy	−1.6	−3.1	−3.2	3.1	7.4		3.7	−41.1	16.2	
Canada	0.5	−10.0	5.3	8.8	0.9		2.5	6.0	0	

Gross National Product [a]

Percent change from previous period seasonally adjusted at an annual rate

	1981	1982	1983	1984	1985	
					1st Qtr	2d Qtr
United States	2.5	−2.1	3.7	6.8	0.3	1.7
Japan	4.1	3.4	3.4	5.7	0.4	
West Germany	−0.2	−1.0	1.3	2.6	−3.1	
France	0.2	2.0	0.7	1.6	−0.2	
United Kingdom	−0.9	1.5	3.1	1.6	2.3	
Italy	0.2	−0.5	−0.4	2.6	2.6	
Canada	3.3	−4.4	3.3	5.0	3.7	

[a] Constant market prices.

Consumer Prices

Percent change from previous period seasonally adjusted at an annual rate

	1981	1982	1983	1984	1985					
					1st Qtr	2d Qtr	Apr	May	Jun	Jul
United States	10.3	6.2	3.2	4.3	3.3	4.2	4.6	2.7	2.6	
Japan	4.9	2.6	1.8	2.3	2.3	1.1	3.0	−1.0	8.7	10.3
West Germany	6.0	5.3	3.3	2.4	3.7	2.6	1.9	1.4	−0.8	−1.3
France	13.3	12.0	9.5	7.7	5.7	6.3	5.9	6.7	6.4	
United Kingdom	11.9	8.6	4.6	5.0	7.0	9.8	12.1	6.0	5.5	
Italy	19.3	16.4	14.9	10.6	10.1	10.5	11.8	9.1	9.3	6.7
Canada	12.5	10.8	5.8	4.3	5.4	3.9	6.3	2.0	3.0	

Money Supply, M-1 [a]

Percent change from previous period seasonally adjusted at an annual rate

	1981	1982	1983	1984	1985					
					1st Qtr	2d Qtr	Apr	May	Jun	Jul
United States [b]	7.1	6.6	11.2	6.9	10.9	10.6	6.3	14.7	21.7	
Japan	3.7	7.1	3.0	2.9	11.1	-7.9	-44.4	7.0	-23.5	
West Germany	1.1	3.6	10.3	3.3	1.4	-0.4	-9.0	-1.2	6.8	
France	12.2	13.9	10.0	7.5	12.7					
United Kingdom	NA	NA	13.0	14.7	1.2	32.4	41.8	32.4	61.2	
Italy	11.2	11.6	15.2	12.0	20.4		17.9			
Canada	3.8	0.7	10.2	3.3	2.5	3.7	-11.3	27.6	1.4	14.3

[a] Based on amounts in national currency units.
[b] Including M1-A and M1-B.

Unemployment Rate [a]

Percent seasonally adjusted

	1981	1982	1983	1984	1985					
					1st Qtr	2d Qtr	Apr	May	Jun	Jul
United States	7.5	9.6	9.5	7.4	7.2	7.2	7.2	7.2	7.2	7.2
Japan	2.2	2.4	2.7	2.7	2.5	2.5	2.4	2.5	2.6	
West Germany	5.6	7.7	9.2	9.1	9.2	9.4	9.4	9.4	9.5	9.5
France	7.6	8.4	8.6	9.6	10.1	10.1	10.0	10.0	10.1	10.2
United Kingdom	10.0	11.6	12.4	12.6	12.9	13.1	13.0	13.1	13.2	13.2
Italy	8.4	9.1	9.9	10.4	10.8	10.2				
Canada	7.5	11.1	11.8	11.3	11.1	10.6	10.9	10.5	10.5	10.4

[a] Unemployment rates for France are estimated.

Foreign Trade [a]

Billion US $, f.o.b.

	1981	1982	1983	1984	1985 1st Qtr	1985 2d Qtr	1985 Apr	1985 May	1985 Jun
United States [b]									
Exports	233.5	212.3	200.7	217.6	55.7	52.6	17.8	17.4	17.4
Imports	261.0	244.0	258.2	325.6	84.4	86.4	28.3	28.7	29.4
Balance	−27.5	−31.6	−57.5	−107.9	−28.7	−33.8	−10.5	−11.3	−12.0
Japan									
Exports	149.6	138.3	145.5	168.2	40.3	42.5	14.2	14.4	13.9
Imports	129.5	119.7	114.1	124.1	28.7	29.5	10.4	9.7	9.4
Balance	20.1	18.6	31.5	44.1	11.5	13.0	3.8	4.7	4.5
West Germany									
Exports	175.4	176.4	169.4	171.9	41.1	42.9	14.5	14.5	13.9
Imports [c]	163.4	155.3	152.9	153.1	36.5	36.9	12.4	12.4	12.1
Balance	11.9	21.1	16.6	18.8	4.6	6.0	2.1	2.1	1.8
France									
Exports	106.3	96.4	95.1	97.5	22.5	24.4	8.2	8.0	8.1
Imports	115.6	110.5	101.0	100.3	23.6	24.7	8.7	8.1	7.9
Balance	−9.3	−14.0	−5.9	−2.8	−1.1	−0.4	−0.4	−0.1	0.2
United Kingdom									
Exports	102.5	97.1	92.1	93.7	22.7	25.4	8.5	8.5	8.3
Imports	94.6	93.1	93.8	99.2	24.2	25.7	8.9	8.2	8.6
Balance	7.9	4.0	−1.8	−5.5	−1.5	−0.4	−0.3	0.3	−0.3
Italy									
Exports	75.4	74.0	72.8	73.6	17.7		5.5	6.6	
Imports	91.2	86.8	80.6	84.3	21.5		7.1	7.4	
Balance	−15.9	−12.8	−7.9	−10.8	−3.8		−1.6	−0.7	
Canada									
Exports	70.5	68.5	73.7	86.8	22.0	21.8	7.4	7.3	7.1
Imports	64.4	54.1	59.3	70.8	18.0	18.1	5.8	6.1	6.2
Balance	6.1	14.4	14.4	16.1	4.0	3.7	1.6	1.2	0.9

[a] Seasonally adjusted.
[b] Imports are customs values.
[c] Imports are c.i.f.

Current Account Balance [a]

Billion US $

	1981	1982	1983	1984	1985 1st Qtr	1985 2d Qtr	1985 Apr	1985 May	1985 Jun
United States	6.3	−9.2	−41.6	−101.5	−30.0				
Japan	4.8	6.9	20.8	35.0	6.8	13.3	4.1	3.6	5.6
West Germany	−6.8	3.3	4.2	6.0	1.7	3.0	1.3	2.0	−0.2
France	−4.7	−12.1	−4.6	−0.2	−0.7				
United Kingdom	15.3	8.5	4.5	0.9	0.1	1.5	0.3	0.9	0.3
Italy	−8.6	−5.7	0.6	−3.2					
Canada	−5.0	2.1	1.4	1.9	0.5				

[a] Seasonally adjusted; converted to US dollars at current market rates of exchange.

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Export Prices in US $

Percent change from previous period at an annual rate

	1981	1982	1983	1984	1985				
					1st Qtr	Mar	Apr	May	Jun
United States	9.2	1.5	1.0	1.4	0	7.3	−6.2	9.7	6.3
Japan	5.5	−6.4	−2.4	0.2	−11.9	−11.2	93.0	−20.0	
West Germany	−14.9	−2.8	−3.2	−7.1	−18.9	4.0	119.6	−2.6	18.5
France	−12.0	−5.5	−4.8	−2.9	−13.5	24.8	116.3	−4.2	
United Kingdom	NA	NA	−6.2	−5.1	−16.2	68.7	174.6	−5.4	23.8
Italy	−7.8	−3.0	−4.4	−5.2	−13.1	−1.8			
Canada	3.9	−2.0	−1.3	−3.7	−0.4	−8.9	12.0	−16.1	−10.6

Import Prices in US $

Percent change from previous period at an annual rate

	1981	1982	1983	1984	1985				
					1st Qtr	Mar	Apr	May	Jun
United States	5.3	−2.0	−3.7	1.7	−10.6	−7.2	1.4	11.5	−9.7
Japan	3.6	−7.4	−5.0	−2.8	−10.9	19.2	−7.2	−2.1	
West Germany	−8.6	−4.7	−5.2	−4.8	−12.9	22.1	76.0	−6.8	−1.9
France	−7.8	−7.2	−7.0	−3.8	−10.9	32.7	77.5	−32.6	
United Kingdom	NA	NA	−5.7	−4.6	−15.4	60.2	158.3	−19.4	11.1
Italy	1.0	−5.3	−6.6	−3.7	−7.9	12.3			
Canada	8.7	−1.1	−3.3	−0.1	−4.7	−7.9	11.9	10.5	−2.7

Exchange Rate Trends

Percent change from previous period at an annual rate

	1981	1982	1983	1984	1985 1st Qtr	2d Qtr	May	Jun	Jul
Trade-Weighted									
United States	10.5	10.6	5.8	9.1	26.0		6.9		
Japan	9.3	–5.7	10.4	6.2	0.9		1.6		
West Germany	–2.1	7.0	5.8	1.0	–0.2		–3.9		
France	–5.1	–6.1	–4.7	–2.1	0.9		1.5		
United Kingdom	2.5	–2.1	–5.0	–2.5	–10.5		17.2		
Italy	–9.2	–5.1	–1.6	–3.1	1.3		0.1		
Canada	0.3	0.2	2.3	–2.3	– 2.1		–8.2		
Dollar Cost of Foreign Currency									
Japan	2.7	–12.9	4.6	0	–19.6	9.9	0.5	12.5	31.2
West Germany	–24.6	–7.2	–5.2	–11.5	–28.0	19.0	–4.3	14.6	46.0
France	–28.7	–20.8	–15.9	–14.7	–26.7	19.6	–5.5	15.7	47.7
United Kingdom	–13.2	–13.4	–13.3	–11.9	–28.6	59.9	10.5	35.5	142.2
Italy	–32.8	–18.8	–12.3	–15.6	–30.3	9.5	–2.9	14.7	30.6
Canada	–2.5	–2.9	0.1	–5.1	–10.5	–5.0	–9.3	6.7	12.5

Money Market Rates

Percent

	1981	1982	1983	1984	1985 1st Qtr	2d Qtr	Apr	May	Jun
United States 90-day certificates of deposit, secondary market	16.24	12.49	9.23	10.56	8.76	8.61	8.61		
Japan loans and discounts (2 months)	7.79	7.23	NA	6.66	6.55	6.54	6.55	6.55	6.53
West Germany interbank loans (3 months)	12.19	8.82	5.78	5.96	6.12	5.98	5.98		
France interbank money market (3 months)	15.47	14.68	12.51	11.74	10.64	10.58	76		
United Kingdom sterling interbank loans (3 months)	13.85	12.24	10.12	9.91	12.98	12.67	12.67		
Italy Milan interbank loans (3 months)	20.13	20.15	18.16	15.91	15.78	15.37	15.37		
Canada finance paper (3 months)	18.46	14.48	9.53	11.30	10.59				
Eurodollars 3-month deposits	16.87	13.25	9.69	10.86	9.04	8.74	8.86	8.61	

Agricultural Prices

	1980	1981	1982	1983	1984	1985				
						1st Qtr	2d Qtr	May	Jun	Jul
Bananas Fresh imported, (Total world, $ per metric ton)	177	214	217	232	243	110.4	111.6	112.0	110.6	NA
Beef (¢ per pound)										
Australia (Boneless beef, f.o.b., US Ports)	125.2	112.1	108.4	110.7	101.1	100.2	93.3	93	92.4	92.9
United States (Wholesale steer beef, midwest markets)	104.3	100.0	101.4	97.6	100.9	96.6	88.9	89.4	88.1	84.2
Cocoa (¢ per pound)	113.5	89.8	74.3	92.1	106.2	99.2	96.4	96.1	91.5	95.7
Coffee ($ per pound)	1.54	1.28	1.40	1.32	1.44	1.44	1.42	1.43	1.42	1.34
Corn (US #3 yellow, c.i.f. Rotterdam $ per metric ton)	150	150	123	148	150	133	133	133	129	126
Cotton (World Cotton Prices, "B" index, c.i.f. Europe, US ¢/lb.)	81.70	75.96	62.87	72.86	75.03	57.95	55.35	55.13	52.60	49.22
Palm Oil (United Kingdom 5% bulk, c.i.f., $ per metric ton)	583	571	445	502	730	605	606	610	556	499
Rice ($ per metric ton)										
US (No. 2, milled, 4% c.i.f. Rotterdam)	598	632	481	514	514	496	496	496	495	488
Thai SWR (100% grade B c.i.f. Rotterdam)	522	573	362	339	310	254	243	250	237	230
Soybeans (US #2 yellow, c.i.f. Rotterdam $ per metric ton)	296	288	244	282	283	240	236	235	229	223
Soybean Oil (Dutch, f.o.b. ex-mill, $ per metric ton)	598	507	447	527	727	651	658	652	630	575
Soybean Meal (US, c.i.f. Rotterdam $ per metric ton)	257	252	219	238	197	157	147	145	142	152
Sugar (World raw cane, f.o.b. Caribbean Ports, spot prices ¢ per pound)	29.03	16.93	8.42	8.49	5.18	3.69	2.96	2.77	2.74	3.15
Tea Average Auction (London) (¢ per pound)	101.4	91.0	89.9	105.2	156.6	126.9	82.8	75.2	74.6	72.6
Wheat (US #2. DNS Rotterdam c.i.f. $ per metric ton)	209	210	187	183	182	177	169	171	166	157
Food Index [a] (1975=100)	232	203	167	184	194	176	168	165	166	161

Industrial Materials Prices

	1980	1981	1982	1983	1984	1985				
						1st Qtr	2d Qtr	May	Jun	Jul
Aluminum (¢ per pound)										
Major US producer	71.6	77.3	76.0	77.7	81.0	81.0	81.0	81.0	81.0	81.0
LME cash	80.8	57.4	44.9	65.1	56.8	49.2	49.3	50.4	47.5	45.7
Chrome Ore (South Africa chemical grade, $ per metric ton)	55.0	53.0	50.9	50.0	50.0	49.9	44.7	43.2	41.0	41.0
Copper [a] (bar, ¢ per pound)	98.7	79.0	67.1	72.0	62.4	62.1	67.6	70.0	65.7	66.0
Gold ($ per troy ounce)	612.1	460.0	375.5	424.4	360.0	300.0	319.8	317.5	315.7	315.8
Lead [a] (¢ per pound)	41.1	32.9	24.7	19.3	20.0	17.2	17.3	17.1	17.4	18.0
Manganese Ore (48% Mn, $ per long ton)	78.5	82.1	79.9	73.3	69.8	69.6	68.4	68.4	68.4	68.4
Nickel ($ per pound)										
Cathode major producer	3.5	3.5	3.2	3.2	3.2	3.2	3.2	3.2	3.2	3.2
LME Cash	3.0	2.7	2.2	2.1	2.2	2.2	2.5	2.5	2.5	2.3
Platinum ($ per troy ounce)										
Major producer	439.5	475.0	475.0	475.0	475.0	475.0	475.0	475.0	475.0	475.0
Metals week, New York dealers' price	677.0	446.0	326.7	422.6	358.2	269.3	275.4	274.6	265.5	267.6
Rubber (¢ per pound)										
Synthetic [b]	40.6	47.5	45.7	44.0	44.4	46.6	45.7	45.8	45.1	NA
Natural [c]	73.8	56.8	45.4	56.2	49.6	42.0	41.5	41.0	41.6	41.5
Silver ($ per troy ounce)	20.7	10.5	7.9	11.4	8.1	5.9	6.3	6.3	6.2	6.0
Steel Scrap [d] ($ per long ton)	91.2	92.0	63.1	73.2	86.4	83.7	71.9	70.2	66.3	NA
Tin [a] (¢ per pound)	761.3	641.4	581.6	590.9	556.6	501.1	541.3	536.0	556.6	575.7
Tungsten Ore (contained metal, $ per metric ton)	18,219	18,097	13,426	10,177	10,243	11,515	10,974	10,832	10,195	10,164
US Steel (finished steel, composite, $ per long ton)	486.2	543.5	567.3	590.2	611.61	617.83	617.83	617.83	617.83	NA
Zinc [a] (¢ per pound)	34.4	38.4	33.7	34.7	41.5	40.0	39.5	40.3	36.8	35.0
Lumber Index [e] (1975=100)	167	159	140	190	176	167	179	183	189	182
Industrial Materials Index [f] (1975=100)	184	166	142	152	138	122.7	124.6	124.0	124	123

[a] Approximates world market price frequently used by major world producers and traders, although only small quantities of these metals are actually traded on the LME.
[b] S-type styrene, US export price.
[c] Quoted on New York market.
[d] Average of No. 1 heavy melting steel scrap and No. 2 bundles delivered to consumers at Pittsburgh, Philadelphia, and Chicago.
[e] This index is compiled by using the average of 11 types of lumber whose prices are regarded as bellwethers of US lumber construction costs.
[f] The industrial materials index is compiled by *The Economist* for 18 raw materials which enter international trade. Commodities are weighted by 3-year moving averages of imports into industrialized countries.

World Crude Oil Production Excluding Natural Gas Liquids

Thousand b/d

	1980	1981	1982	1983	1984	1985				
						1st Qtr	Feb	Mar	Apr	May
World	**59,463**	**55,827**	**53,014**	**52,588**	**53,827**	**53,028**	**53,506**	**53,743**	**53,616**	**52,394**
Non-Communist countries	**45,243**	**41,602**	**38,810**	**38,228**	**39,257**	**38,756**	**39,236**	**39,473**	**39,077**	**37,554**
Developed countries	12,859	12,886	13,276	13,864	14,302	14,693	14,709	14,800	14,772	14,893
United States	8,597	8,572	8,658	8,680	8,735	8,871	8,911	8,968	8,907	9,032
Canada	1,424	1,285	1,270	1,356	1,411	1,463	1,463	1,507	1,467	1,475
United Kingdom	1,619	1,811	2,094	2,299	2,535	2,660	2,650	2,600	2,621	2,598
Norway	528	501	518	614	700	719	705	755	765	765
Other	691	717	736	915	921	980	980	970	1,012	1,023
Non-OPEC LDCs	5,443	6,036	6,633	6,823	7,515	7,788	7,744	7,949	7,984	7,912
Mexico	1,936	2,321	2,746	2,666	2,746	2,711	2,687	2,810	2,820	2,792
Egypt	595	598	665	689	827	916	925	935	915	900
Other	2,912	3,117	3,222	3,468	3,942	4,161	4,132	4,204	4,249	4,220
OPEC	26,941	22,680	18,901	17,541	17,440	16,275	16,783	16,724	16,321	14,749
Algeria	1,020	803	701	699	638	660	665	690	650	650
Ecuador	204	211	211	236	253	274	277	277	256	280
Gabon	175	151	154	157	152	150	150	150	150	150
Indonesia	1,576	1,604	1,324	1,385	1,466	1,152	1,155	1,152	1,150	1,150
Iran	1,662	1,381	2,282	2,492	2,187	2,097	2,200	2,300	2,500	2,200
Iraq	2,514	993	972	922	1,203	1,300	1,300	1,300	1,300	1,300
Kuwait [b]	1,389	947	663	881	912	914	1,000	850	800	800
Libya	1,830	1,137	1,183	1,076	1,073	1,034	1,000	1,100	1,100	1,100
Neutral Zone [c]	544	370	317	390	410	480	480	500	400	330
Nigeria	2,058	1,445	1,298	1,241	1,393	1,590	1,680	1,700	1,600	1,400
Qatar	471	405	328	295	399	292	280	315	300	290
Saudi Arabia [b]	9,631	9,625	6,327	4,867	4,444	3,659	3,900	3,700	3,400	2,500
UAE	1,702	1,500	1,248	1,119	1,097	1,123	1,106	1,155	1,555	1,161
Venezuela	2,165	2,108	1,893	1,781	1,813	1,550	1,590	1,535	1,560	1,538
Communist countries	**14,220**	**14,238**	**14,289**	**14,396**	**14,417**	**14,272**	**14,270**	**14,270**	**14,539**	**14,840**
USSR	11,700	11,800	11,830	11,864	11,728	11,402	11,400	11,400	11,639	11,940
China	2,113	2,024	2,044	2,120	2,280	2,450	2,450	2,450	2,480	2,480
Other	407	414	415	412	409	420	420	420	420	420

[a] Preliminary.
[b] Excluding Neutral Zone production, which is shown separately.
[c] Production is shared equally between Saudi Arabia and Kuwait.

Big Seven: Inland Oil Consumption

Thousand b/d

	1980	1981	1982	1983	1984	1985				
						1st Qtr	Mar	Apr	May	Jun
United States [a]	17,006	16,058	15,296	15,184	15,708	15,813	15,321	15,345	15,460	15,276
Japan	4,674	4,444	4,204	4,193	4,349	4,720	4,483	3,754		
West Germany	2,356	2,120	2,024	2,009	2,012	1,993	1,815	2,013		
France	1,965	1,744	1,632	1,594	1,531	1,766	1,561	1,390	1,288	1,293
United Kingdom	1,422	1,325	1,345	1,290	1,624	1,881	1,613			
Italy [b]	1,602	1,705	1,618	1,594	1,513	1,715	1,573	1,368	1,257	
Canada	1,730	1,617	1,454	1,354	1,348	1,343	1,244	1,269		

[a] Including bunkers, refinery fuel, and losses.
[b] Principal products only prior to 1981.

Big Seven: Crude Oil Imports

Thousand b/d

	1980	1981	1982	1983	1984	1985				
						1st Qtr	Mar	Apr	May	Jun
United States	5,220	4,406	3,488	3,329	3,402	2,545	2,808	3,401	3,488	3,301
Japan	4,373	3,919	3,657	3,567	3,664	3,777	4,083	3,270	3,607	
West Germany	1,953	1,591	1,451	1,307	1,335	1,419	1,529	1,242		
France	2,182	1,804	1,596	1,429	1,395	1,578	1,701	1,469	1,139	
United Kingdom	893	736	565	456	482	534	671			
Italy	1,860	1,816	1,710	1,532	1,507					
Canada	557	521	334	247	244	189	177			

OPEC: Crude Oil Official Sales Price [a]

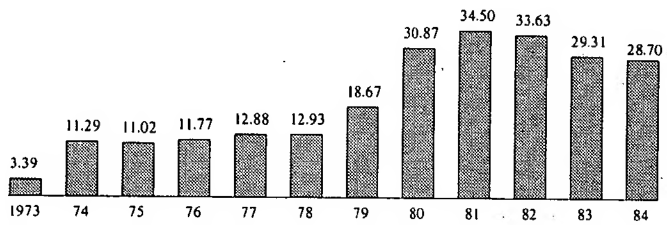
US $ per barrel

	1979	1980	1981	1982	1983	1984	1985			
							1st Qtr	2d Qtr	Jun	Jul
OPEC average [b]	18.67	30.87	34.50	33.63	29.31	28.70	28.25	28.11	28.12	28.00
Algeria 42° API 0.10% sulfur	19.65	37.59	39.58	35.79	31.30	30.50	30.15	29.50	29.50	29.50
Ecuador 28° API 0.93% sulfur	22.41	34.42	34.50	32.96	27.59	27.50	26.82	26.50	26.50	26.15
Gabon 29° API 1.26 % sulfur	18.20	31.09	34.83	34.00	29.82	29.00	28.35	28.00	28.00	28.00
Indonesia 35° API 0.09% sulfur	18.35	30.55	35.00	34.92	29.95	29.53	28.88	28.53	28.53	28.53
Iran										
Light 34° API 1.35% sulfur	19.45	34.54	36.60	31.05	28.61	28.00	28.38	28.05	28.05	28.05
Heavy 31° API 1.60% sulfur	18.49	33.60	35.57	29.15	27.44	27.10	27.41	27.35	27.35	27.35
Iraq [c] 35° API 1.95% sulfur	18.56	30.30	36.66	34.86	30.32	29.43	28.78	28.43	28.43	28.43
Kuwait 31° API 2.50% sulfur	18.48	29.84	35.08	32.30	27.68	27.30	27.30	27.30	27.30	27.30
Libya 40° API 0.22% sulfur	21.16	36.07	40.08	35.69	30.91	30.40	30.40	30.40	30.40	30.40
Nigeria 34° API 0.16% sulfur	20.86	35.50	38.48	35.64	30.22	29.12	28.24	28.37	28.37	28.37
Qatar 40° API 1.17% sulfur	19.72	31.76	37.12	34.56	29.95	29.49	28.48	28.10	28.10	28.10
Saudi Arabia										
Berri 39° API 1.16% sulfur	19.33	30.19	34.04	34.68	29.96	29.52	28.48	28.11	28.11	28.11
Light 34° API 1.70% sulfur	17.26	28.67	32.50	34.00	29.46	29.00	28.32	28.00	28.00	28.00
Medium 31° API 2.40% sulfur	16.79	28.12	31.84	32.40	27.86	27.40	27.48	27.40	27.40	27.20
Heavy 27° API 2.85% sulfur	16.41	27.67	31.13	31.00	26.46	26.00	26.50	26.50	26.50	26.00
UAE 39° API 0.75% sulfur	19.81	31.57	36.42	34.74	30.38	29.56	28.52	28.15	28.15	28.15
Venezuela 26° API 1.52% sulfur	17.22	28.44	32.88	32.88	28.69	27.88	27.69	27.60	27.60	27.10

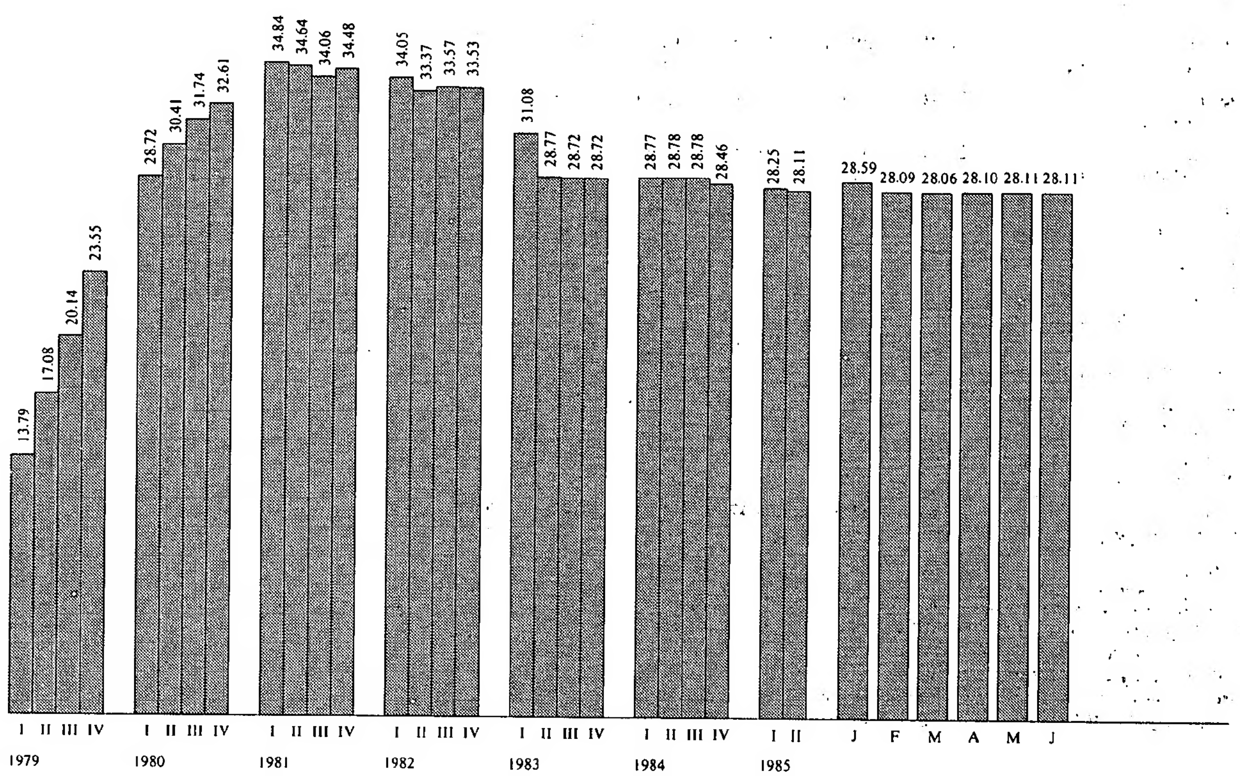
[a] F.o.b. prices set by the government for direct sales and, in most cases, for the producing company buy-back oil.
[b] Weighted by the volume of production.
[c] Beginning in 1981 the price of Kirkuk (Mediterranean) is used in calculating the OPEC average official sales price.

OPEC: Average Crude Oil Sales Price

US $ per barrel



Annual average



The 1973 price is derived from posted prices, not official sales prices.

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